BANCA D'ITALIA

ABRIDGED VERSION OF THE

REPORT

FOR THE YEAR

1964

PRESENTED TO THE

ORDINARY GENERAL MEETING OF SHAREHOLDERS

HELD IN ROME ON 31 MAY, 1965

ROME
PRINTING OFFICE OF THE BANCA D'ITALIA
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REPORT OF THE GOVERNOR

I. *General Economic Conditions, International Liquidity Problems*

The course of economic events in the Western world last year demonstrated clearly that today the major problems of each separate nation, their solution and, to a large extent, also the choice of policies, are matters of concern to the whole international community. Interdependence is most patent where the economic relations between countries rest on institutional arrangements tending toward supranational ends.

In this situation the freedom of action of government in the economic field is subject to limitations which it is hard not to observe. The margins of time and amplitude within which the nations are free to choose the objects of their economic policy are narrowing, and this applies equally to the choice of means — that is, to monetary, fiscal and incomes policy.

The Present Outlook.— Many problems come to mind in the context of international economic interdependence: the persistent disparity of cyclical phases in various countries, the United States balance-of-payments deficit and its repercussions on U.S. relations with Western Europe and the working of the international monetary system, the sterling crisis, destabilizing short-term capital movements between industrial countries, the progress of inflation in Europe and the difficulty of containing the rise of money wages within the limits of productivity increases, the prospect of slower growth in the major industrial countries. These are the problems which at present show up most clearly how close the economic interdependence of the international community is getting to be, and it is to them that governments and central banks direct their efforts separately and jointly in each country and in collaboration between countries.

In the European Economic Community (EEC) as a whole gross domestic product still grew at a faster rate last year than in 1963 (5.5 as against 3.9 per cent), thanks largely to a few typically cyclical factors which had a strong expansionary effect on demand especially during the first half of the year. In addition, better weather conditions made room for more elasticity of supply in building and agriculture. Almost everywhere investment demand and foreign demand contributed most to income formation, while the expansion of public and private consumption alike slowed down.

But this general picture hides great disparities in the actual movement of the demand components in various countries and in the timing of cyclical phases; it also conceals a certain general deceleration during the last few months of the year. Moreover, the Italian economy followed a pattern all its own, both as regards the year's overall results and the behaviour of the different components of demand and supply in the course of the year.

The cyclical disparities within the European Economic Community are in the last resort due to the fact that integration so far really encompasses only commercial policy and has not as yet reached the stage of effectively common decision-making in economic and financial policy.

Experiences in the United Kingdom and the United States no less than in the EEC itself all underline how difficult it is to reconcile the fundamental objectives of economic policy on the domestic level. In a system of fixed exchange rates and free trade, currency reserves are a limiting factor, and for this reason high growth rates and full employment had, at least for some time and to some extent, to be sacrificed to the objective of re-equilibrating the balance of payments through price stabilization. In the event, this objective was not in all cases considered as overriding; in trying to relaunch the economy, the authorities of some Member States again have to take certain risks, because they cannot be sure of being able to control money incomes.

Another lesson of experience is that under the current system of wage negotiations and agreements wages tend to rise more than productivity, and that this tendency is harder to control in countries or sectors where sliding scales are in force. Only the United States and Germany managed to contain the pressure of wages. Notwithstanding repeated recommendations on the part of EEC and the Organisation for Economic Co-operation and Development (OECD), no other country has so far succeeded in defining an effective incomes policy even in the context of a national plan. Should the economy come under strain once more, most countries may therefore be forced either to interrupt or slow down the growth process or else to let prices rise and the balance of payments deteriorate—which would not avert the end result, but would only make it worse. As it happened, the events of 1964 have proved that an upward pressure on wage rates can be associated with falling demand, and that this inconsistency has a seriously depressing effect on the level of employment and hence on the purchasing power of wage earners. In the recent experience of the European Economic Community, wages policy has acquired more weight as an inflationary factor as inflationary impulses from abroad diminished.

International Financial Co-operation.— Last year again, international financial co-operation proved one of the most effective means of solving pressing problems. This applies to all the international organizations and arrangements of which the industrial countries form part. All nations are becoming increasingly aware that interests other than their own need to be taken into account in whatever they do, and that any unilateral action harmful to those other interests meets with universal disapprobation. In addition, countries members of the EEC tend to adjust their conduct more and more to the supranational principles of the Rome Treaty; in the monetary field, this ultimately means an approach to currency union, even if it is still considered premature now.

But there were certainly also some steps backward last year, witness the United Kingdom's introduction of a 15 per cent surcharge on imports, restrictions on the free movement of capital either through fiscal measures (the U.S. interest equalization tax and the 25 per cent withholding tax on dividends in Germany) or through physical controls, and the unilateral positions taken up with respect to the working of the international monetary system. Nevertheless, interdependence between the economies of separate countries has now become so close that economic events in any one country, as well as its measures of economic and more especially monetary policy, have an immediate effect upon the situation of all other members of the international community. It need only be recalled how quickly inflationary pressures spread throughout the EEC in consequence of the imbalance experienced in Italy, France and the Netherlands in 1963 and early in 1964; other examples are the effect which the persistent weakness of the reserve currencies has on Europe, and the repercussions of recent U.S. measures on European markets.

Imported inflation, that is, the propagation of inflationary impulses through the mechanism of the balance of payments, is apt to create very difficult problems for the countries at the receiving end. If an external surplus directly pushes up domestic demand, as happens when the surplus comes from current transactions or direct investment, then the instruments by which monetary authorities normally control and contain domestic liquidity are much less effective than when the surplus arises from purely financial transactions. In both cases, moreover, it is hard to persuade public opinion that corrective measures need to be taken when the balance of payments is so patently in surplus.

Yet the studies conducted by the Group of Ten last year stressed the dangers of delay in making use of these instruments. Each government individually, it is argued, should take responsibility for reconciling its own social priorities with the need for external equilibrium, as well as for making sure that it is fully equipped with the policy instruments necessary to its task. It is along this line of thought that the Ministers and Governors of the Ten invited Working Party no. 3 of the OECD to examine whether and how member nations could, individually and jointly, in the future preserve a better balance-of-payments equilibrium and achieve a faster and more effective adjustment of imbalance; the study was to cover also the measures and instruments best adapted to this purpose.

Co-operation to finance imbalances rests on the idea that a deficit country cannot, and should not, ever rely with absolute certainty on being able to raise the means to finance its deficit, but that the provision of finance should be conditional upon a domestic adjustment programme approved by the lender countries either as a group or through the international organizations to which they belong. It follows that the amount and duration of financial aid accorded to any country should be such as to allow its own corrective measures to take effect gradually, without a sudden shock which would jeopardize the fundamental objectives of domestic economic policy and without detriment to the processes of integration, the flow of transactions and the expansion of world trade.

In 1964, as before, balance-of-payments disequilibria were financed by multilateral and bilateral medium-term credits and by mutual credit facilities between governments and central banks; to some extent, deficits were financed also by accumulating reserve currencies.

The choice of the method of financing depended largely upon the particular moment's circumstances and political opportunities. Nevertheless, the conviction has gained ground that it is conducive to more durable effects if the instruments of financing an external imbalance are chosen in the light of its nature. A deficit on current account not made good by a net inflow of long-term capital, or a deficit due to long-term capital export in excess of the current surplus, implies increased pressure on the real resources of third countries. Imbalances of this kind ought not to be financed by monetary means. Conversely, an external deficit caused by short-term capital movements (anticipated or deferred settlement of commercial transactions, speculative movements of funds, bank credits, etc.) or by sudden shifts in security investments may, within limits, be financed by credits which are to a certain extent automatic, such as those which have become customary in recent years between governments and central banks.

The network of bilateral and multilateral credit facilities specially designed to meet speculative movements or sudden pressures has become an important part of the international monetary system. The Ministers and Governors of the Group of Ten have agreed to participate, through the international institutions to which they belong, in a multilateral surveillance of the ways and means of financing balance-of-payments disequilibria. Such surveillance appeared all the more necessary as the range of financing means includes not only short-term credit facilities on a normally bilateral basis (swaps, bonds denominated in the creditor country's currency, other special support measures), but also funds from the Euro-currency markets. These can be borrowed abroad by commercial banks and used, instead of reserves, to cover a deficit, and the whole matter then escapes the control of other countries.

Co-operation in defense of the stability of the international monetary system was especially active in 1964 and in the early months of the current year. Countries continued to honour their undertakings with respect to control of the London gold market, the EEC defined procedures to be applied in case any Member State wished to modify its rate of exchange, a unit of account was adopted as an expression of agricultural prices within the European Economic Community, and, last but not least, both the International Monetary Fund and the Group of Ten reviewed the conditions best apt to promote the orderly progress of the international monetary system.

The EEC countries' decision in April 1964 to the effect that any Member State may alter its exchange parity only subject to prior consultations was followed up a year later, on 1 April 1965, by the entry into force of the procedures for such consultation.

Member States in effect acknowledge that if any one of them were to alter its exchange rate, this would affect the rest of them more directly and more strongly than it would affect third countries. The same view was evident in the discussions which preceded the decision to express the prices of some agricultural products in units of account rather than in national currencies, as well as the proposals which the monetary committee submitted to the Council of Ministers concerning the definition of this unit of account. These discussions made it clear that, while the mere adoption of a unit of account did not necessarily preclude parity changes as an instrument of monetary policy, they would become more difficult as uniform prices were established for a growing number of products.

The Problems of International Liquidity.— Two studies have been conducted on the functioning of the international monetary system and its ability to provide for an orderly increase in liquidity reserves in line with the expansion of world trade. One of these studies was made by the International Monetary Fund and the other by the Group of Ten. They both came to hand last August, and they both agree on the value of the system's present structure, based as it is on the established price of gold and fixed exchange rates.

Both studies, too, conclude that there is at present no shortage of liquidity. If anything, it might be said that total reserves throughout the world are too much, thanks to the accumulation of large deficits in the U.S. balance of payments since 1958; but there are regional deficiencies which cannot be met through the traditional credit mechanisms. The only mention which the Group of Ten made of this matter in their report, was to recall that it was suggested during the discussions that longer-term lending for monetary purposes might be in the general interest.

Through all the divergent views which have been put forward, a consensus of opinion seems to be emerging slowly to the effect that international liquidity creation should not be allowed to depend upon balance-of-payments deficits of a reserve-currency country, but should be based on the effective requirements of the international economy. It is obvious that aggregate liquidity needs, while they are no doubt in some way related to the growth of world income and trade, cannot be determined mechanically in terms of the volume of transactions, which is influenced by altogether too many variables.

One symptom of overall reserve shortage might be the growing tendency of monetary authorities in industrial countries to consider it an important objective of their economic policy to increase their reserves. This would end up in a race to accumulate balance-of-payments surpluses and ultimately in a deflationary spiral. However, the process would certainly be associated with widespread use of the credit facilities available at the International Monetary Fund and under other arrangements, and would at least give the members of the international community an idea of just how much reserves are needed and how much liquidity ought to be created.

The question of the qualitative composition of reserves suddenly came into the limelight with France's decision to convert into gold part of her existing foreign exchange balances and all those she was to earn in the future through external surpluses. The same question was touched upon in a number of public pronouncements on the working of the international monetary system.

The French position still needs clarification. In particular, it is not at all obvious whether it should be interpreted as acceptance of the doctrine of a return to the pure gold standard, or whether it implies that the idea to create a collective reserve unit is being dropped and emphasis placed instead on the qualitative aspect of the problem, that is, the composition of reserves.

However that might be, and quite apart from the quantitative aspect of the problems connected with the working of the international monetary system, it is right and proper that now that France has taken up this position, other countries should as soon as possible state where they stand on the issue of the qualititative composition of reserves.

The Group of Ten in their report already made two statements which are relevant in this connection. They say: " gold will continue to be the ultimate international reserve asset and common denominator of par values ", and " the contribution of dollar holdings to the growth in international liquidity seems unlikely to continue as in the past ".

These views are not open to objection, nor can there be anything but full agreement with any move tending to strengthen monetary discipline and to underline the obligation which each and every member of the international community, including reserve centres, has to take care of its own overall balance-of-payments equilibrium. This indeed has been said in Italy more than once before the report of the Group of Ten. Furthermore, there is no gainsaying the disadvantages of making liquidity creation dependent upon deficits in the balance of payments of leading countries rather than upon the effective needs of the whole international system. This is where the multilateral surveillance approved by the Group of Ten finds its place. This system has already begun to be applied, and once it is refined in the light of initial practical experience, it will surely help to bring the world closer to a situation in which the supply of international liquidity ceases to be governed by the deficits of a key-currency country or of some other major industrial nation.

However, like other members of the Group of Ten and of the European Economic Community, Italy cannot accept the principle that the gold exchange standard no longer meets today's realities and should, therefore, be dismantled—even if this is to be done through negotiations within the EEC and the IMF. We believe in the merits of slow evolution and in discussion and reciprocal agreements shaded from the glare of publicity which so upsets the delicate mechanism of the exchange and gold markets.

In particular, Italy cannot accept the principle that central banks should hold their reserves only in the form of gold or gold-based assets. The reserve currencies have a useful function to perform in present conditions, whether it is on the world level like the U.S. dollar, or on a regional level like sterling and the French franc. These currencies have, after all, acquired the properties of a reserve currency not by virtue of some international decision, but through a long process of conditioning. Given that the countries concerned are large and powerful markets of goods, credit, capital and insurance, these currencies came to be used more and more in international trade and payments; they were held first by commercial banks and later also by central banks, which use them not only to intervene in exchange markets but also as a repository of their own reserves. The dollar can continue to be used as a means of intervention in exchange markets, and it can continue to discharge the function of reserve currency together with gold and such other gold-based assets as may be considered necessary in the future.

We oppose the proposal to return to a pure gold standard. We do so not only because it runs counter to modern theory and experience (the gold standard never was an automatic system, but one consciously managed, at least to a large extent, and experience contradicts the existence of any mechanical link between the balance of payments and domestic liquidity); we oppose it also because the manifold needs of the modern world and the complex objectives of economic policy preclude the application of mechanical rules.

Lastly, the progressive elimination of reserve currency holdings in excess of working balances harbours within itself the seeds of deflation and might well undermine the very foundations of the international monetary system. In this light it appears more urgent than ever for the industrial countries to apply a joint policy in the matter of the composition of reserves, as we have long suggested with the more recent support of German leaders.

II. *Economic Conditions in Italy*

For Italy, the year 1964 was one of difficult readjustments. Of the many facets of this process, some at least, like the development of production and prices late in 1964 and early this year, suggest that the country may have begun to emerge from the strains and stresses which have been its lot since 1962.

The upward movement of wages, costs and prices which had been the dominant feature of the preceding two years, was a little slower, but still vigorous enough last year. While wages and prices continued to rise, demand for labour, which in recent years had been strong, slackened appreciably.

Even more than in 1963, the growth rate of gross national product in real terms slowed down again. The already much reduced increase in investment turned into a contraction. Consumption, which in 1963 had expanded almost twice as much as national income, last year virtually kept in step with the latter.

Imports fell, in striking contrast to 1963, when they had soared mainly under the pressure of consumption demand. Exports, on the other hand, expanded much more than in 1963. The preceding year's heavy deficit gave way in 1964 to a quite considerable surplus in the exchange of goods and services with the rest of the world.

As was noted in last year's Annual Report, the sharp increases in wages and costs since 1962 first pushed up consumption and imports, but then depressed investment and exports and so slowed down the growth of national income as of 1963.

Last year the income-depressing effect was more patent still, with investment contracting and employment falling; exports, by contrast, made a vigorous recovery.

Agriculture had a good year, but because industrial expansion came to a halt, gross national product in real terms rose by only 3.0 per cent (at 1954 prices), compared with 5.1 per cent in 1963 and with 6.6 per cent in 1962 (Table 1). This is the lowest increment in the postwar period, with the sole exception of 1952.

Gross investment, which had already been rising at a slower rate for two years, but yet expanded (in real terms, at 1954 prices) by 8.2 per cent in 1962 and by 5.4 per cent in 1963, contracted last year by 11.4 per cent. Directly productive investment actually dropped by 20 per cent, but social investment increased by 6.7 per cent.

Total domestic employment decreased by 0.3 per cent, and employment of dependent labour by 0.7 per cent, after a 2.0 per cent increase in 1963. Some of those who lost their jobs became self-employed and others remained unemployed.

Wage labour in industry (excluding building), which had increased so fast of late, decreased by 2.5 per cent, compared with a rise of 3.4 per cent in 1963. The figures look rather worse in terms of 12-month changes, for then a decrease of 4.2 per cent in the last quarter of 1964 compares with an increase of the same proportion during the last quarter of 1963.

TABLE 1

Italy: Growth of Aggregate Demand and Supply, 1958 to 1964

(Annual percentage variations)

OECD Schedule

Year	Demand					Supply	
	aggregate	domestic			foreign	domestic	foreign
		total	consumption	gross investment	exports of goods and services	gross domestic product	imports of goods and services
A) *At current prices*							
1958	4.9	5.2	6.1	1.6	2.9	7.0	— 8.7
1959	6.6	6.0	4.9	10.0	11.1	6.9	4.8
1960	12.3	10.8	8.0	20.6	21.8	9.0	36.7
1961	10.7	10.0	8.9	13.7	14.6	10.5	12.2
1962	13.1	13.4	13.2	13.9	11.5	12.6	16.1
1963	15.9	16.7	18.4	11.7	11.2	14.3	25.1
1964	7.3	6.1	8.9	— 2.8	14.7	9.3	— 2.6
B) *At 1954 prices*							
1958	3.7	3.6	4.1	1.8	4.0	4.4	— 1.1
1959	7.9	6.6	5.1	11.7	16.6	7.7	9.9
1960	11.0	9.6	6.7	19.2	18.9	7.1	36.9
1961	9.6	8.2	7.2	11.3	16.5	8.4	15.4
1962	8.0	7.4	7.2	8.2	10.6	6.6	14.9
1963	8.0	8.3	9.3	5.4	6.5	5.1	21.1
1964	1.2	— 0.9	2.6	— 11.4	11.0	3.0	— 5.9
C) *Price variations*							
1958	1.2	1.5	1.9	— 0.1	— 1.1	2.5	— 7.7
1959	— 1.2	— 0.6	— 0.2	— 1.5	— 4.7	— 0.7	— 4.6
1960	1.2	1.1	1.2	1.2	2.4	1.8	— 0.1
1961	1.0	1.7	1.6	2.2	1.6	1.9	— 2.8
1962	4.7	5.6	5.6	5.3	0.8	5.6	1.0
1963	7.3	7.8	8.3	6.0	4.4	8.8	3.3
1964	6.0	7.1	6.1	— 9.7	3.3	6.1	3.5

Source: Report on the Economic Situation in Italy.

Industrial output, including building, expanded by only 1.0 per cent last year, after a growth of 8.2 per cent in 1963.

Wage incomes in the aggregate followed up their rise of 17.7 and 22.8 per cent in the preceding two years with a further rise of 12 per cent in 1964.

Wage incomes per head, in their turn, also increased less than in either of the two preceding years. Allowing for the decrease of wage labour and the overall increase in labour incomes, wage earnings per head rose by 12.8 per cent last year, compared with 20.4 and 14.8 per cent, respectively, in 1963 and 1962.

The volume of aggregate consumption increased much less in relative terms than in 1963, the two figures being 2.6 and 9.3 per cent. In terms of absolute value, consumption rose less than disposable incomes, so that net domestic saving rose again after the contraction of 1963. This means a return from a negative to a positive marginal propensity to save.

Imports of goods and services fell last year by 5.9 per cent at constant (1954) prices and by 2.6 per cent at current prices, having risen in 1963 by 21.1 and 25.1 per cent, respectively. Exports on the other hand expanded more than in 1963, the two years' volume figures being 11.0 and 6.5 per cent, and the value figures 14.7 and 11.2 per cent.

Thanks largely to merchandise trade, the 1963 deficit of 616 billion lire on goods and services account turned last year into a surplus of 242 billion.

With the cost push easing somewhat, pressure on prices, though still considerable, was also less. The Central Statistical Institute's index of wholesale prices rose by another 3.4 per cent, to follow the 1963 increase of 5.2 per cent. Retail prices and the cost of living similarly rose less than the year before, the respective figures being 5.9 and 6.5 per cent last year, and 7.5 and 8.8 per cent in 1963.

Thus continuing pressure on prices was associated with a diminution of demand for labour and of employment—obvious proof of the nature of inflation in Italy during the last few years.

The primary effects of the excessive wage rise were, on the one hand, that the great increase in wage incomes generated an exceptional expansion of consumption, and on the other hand, that the profit margins of firms narrowed together with the operating surpluses of corporations and agencies which do not work on the profit motive, so that investment slowed down.

Secondary effects followed in the form of an outright contraction of investment and a diminution of the demand for labour and of employment. In spite of the continuing wage rise, wage income gradually rose less and less, and private consumption slowed down, not least also because of the diminishing propensity to consume.

National expenditure and income both rose at increasingly slower rates, but while prices and wages also rose less, they still rose.

At first, imports soared and exports suffered a setback, so that the balance of payments on goods and services account got deeply into the red. Subsequently, imports fell and exports recovered vigorously, so that the goods and services account returned to surplus in the presence of continuing, though attenuated, price and wage rises.

National Accounts.— Figures on the supply and use of resources, calculated according to the OECD schedule, show gross national product at current prices to have been 30,950 billion lire last year. This is an increase of 9.3 per cent over the 1963 figure of 28,329 billion, but of only 2.7 per cent in terms of 1963 prices (Table 2).

In their turn, resources disposable for domestic uses rose from 28,945 to 30,708 billion lire (both at current prices), which means an increase of 6.1 per cent in value terms and a minimal decline of 0.3 per cent in real terms. It follows that the additional real resources produced by the country went to improve the balance of payments on goods and services account.

Private consumption absorbed 61.6 per cent of the resources disposable for domestic uses, and public consumption another 16.7 per cent; social investment took 9.9 per cent, and the remaining 11.8 per cent were accounted for by directly productive investment (Table 3).

At 24,033 billion lire, total consumption was 8.9 per cent higher (in terms of current prices) than in 1963, private consumption having risen by 7.8 and public consumption by 12.8 per

TABLE 2

Condensed National Accounts

OECD Schedule

Origin and use of resources	Billion lire at current prices (1)		Compo-sition per cent	Percentage change 1964/63 at		Annual average rate of increase at 1954 prices		
	1963	1964	1964	current prices	1963 prices	1950-58	1958-63	1950-63
Origin of resources:								
Value added in agriculture, forestry and fisheries	3,719	3,964	*10.9*	*6.6*	. .	3.9	0.9	2.4
Value added in industry	11,139	12,116	*33.5*	*8.8*	. .	9.0	10.0	6.4
Value added in tertiary activities	7,306	8,023	*22.1*	*9.8*	. .	4.0	6.8	5.2
Value added in public administration	2,987	3,377	*9.3*	*13.1*	. .	3.5	2.8	3.3
Adjustments	– 469	– 429	– *1.2*	– *8.5*	. .	13.3	2.8	8.6
Gross domestic product at factor cost	24,682	27,051	*74.6*	*9.6*	. .	5.8	6.8	6.2
Taxes not included above in the value of goods and services	3,538	3,758	*10.3*	*6.2*	. .	4.0	8.4	5.4
Gross domestic product at market prices	28,220	30,809	*84.9*	*9.2*	. .	5.6	6.9	6.1
Net income from abroad	109	141	*0.4*	*29.4*	. .	18.7	14.5	17.0
Gross national product	28,329	30,950	*85.3*	*9.3*	*2.7*	5.6	6.8	6.1
Imports of goods and services	5,461	5,317	*14.7*	– *2.6*	– *5.9*	8.8	19.3	12.8
Total . . .	33,790	36,267	*100.0*	*7.3*	*1.3*	5.8	5.5	5.8
Use of resources:								
Exports of goods and services	4,845	5,559	*15.3*	*14.7*	*10.9*	11.6	13.7	12.4
Resources disposable for domestic uses	28,945	30,708	*84.7*	*6.1*	– *0.3*	5.3	7.8	6.3
Consumption	22,079	24,033	*66.3*	*8.9*	*2.7*	4.6	7.1	5.6
of which: private	17,543	18,918	*52.2*	*7.8*	*2.4*	4.1	7.4	5.3
public	4,536	5,115	*14.1*	*12.8*	*3.9*	7.9	5.0	6.8
Gross investment	6,866	6,675	*18.4*	– *2.8*	– *10.1*	7.6	10.8	8.8

(1) Source: Report on the Economic Situation in Italy.

TABLE 3

Use of Domestically Disposable Resources

Item	Billion lire at current prices		Composition per cent 1964	Percentage change in		
	1963	1964		volume	price	value
Directly productive investment	4,296	3,637	*11.8*	– *20.0*	*5.9*	– *15.3*
Gross fixed investment	4,071	3,487	*11.3*	– *19.2*	*6.1*	– *14.3*
of which:						
Agriculture	633	553	*1.8*	– *19.1*	*8.0*	– *12.6*
Industry and services	3,438	2,934	*9.5*	– *19.2*	*5.6*	– *14.7*
Stocks	225	150	*0.5*	—	—	—
Social uses	7,106	8,153	*26.6*	*4.9*	*9.3*	*14.7*
of which:						
Public consumption	4,536	5,115	*16.7*	*3.9*	*8.6*	*12.8*
Social investment	2,570	3,038	*9.9*	*6.7*	*10.8*	*18.2*
Private consumption	17,543	18,918	*61.6*	*2.4*	*5.3*	*7.8*
Total	28,945	30,708	*100.0*	– *0.3*	*6.4*	*6.1*

Source: Report on the Economic Situation in Italy.

cent. In real terms, private consumption went up by 2.4 and public consumption by 3.9 per cent, the respective prices having risen by 5.3 and 8.6 per cent.

Social investment amounted to 3,038 billion lire last year as against 2,570 billion in 1963. This increase of 18.2 per cent in monetary and of 6.7 in real terms, compares with a contraction of 15.3 and 20.0 per cent, respectively, in directly productive investment, which absorbed only 3,637 billion lire as against 4,296 billion in 1963 (Table 4).

The fall in industrial investment was spread over virtually all branches, with the sole exception of steel and electricity.

Gross national saving rose by 10.3 per cent from 6,428 to 7,090 billion lire. This was more than gross domestic investment, so that Italy accumulated a foreign credit balance of 415 billion lire—in striking contrast to 1963, when domestic investment exceeded gross national saving and foreign debts in the amount of 438 billion lire were incurred.

TABLE 4

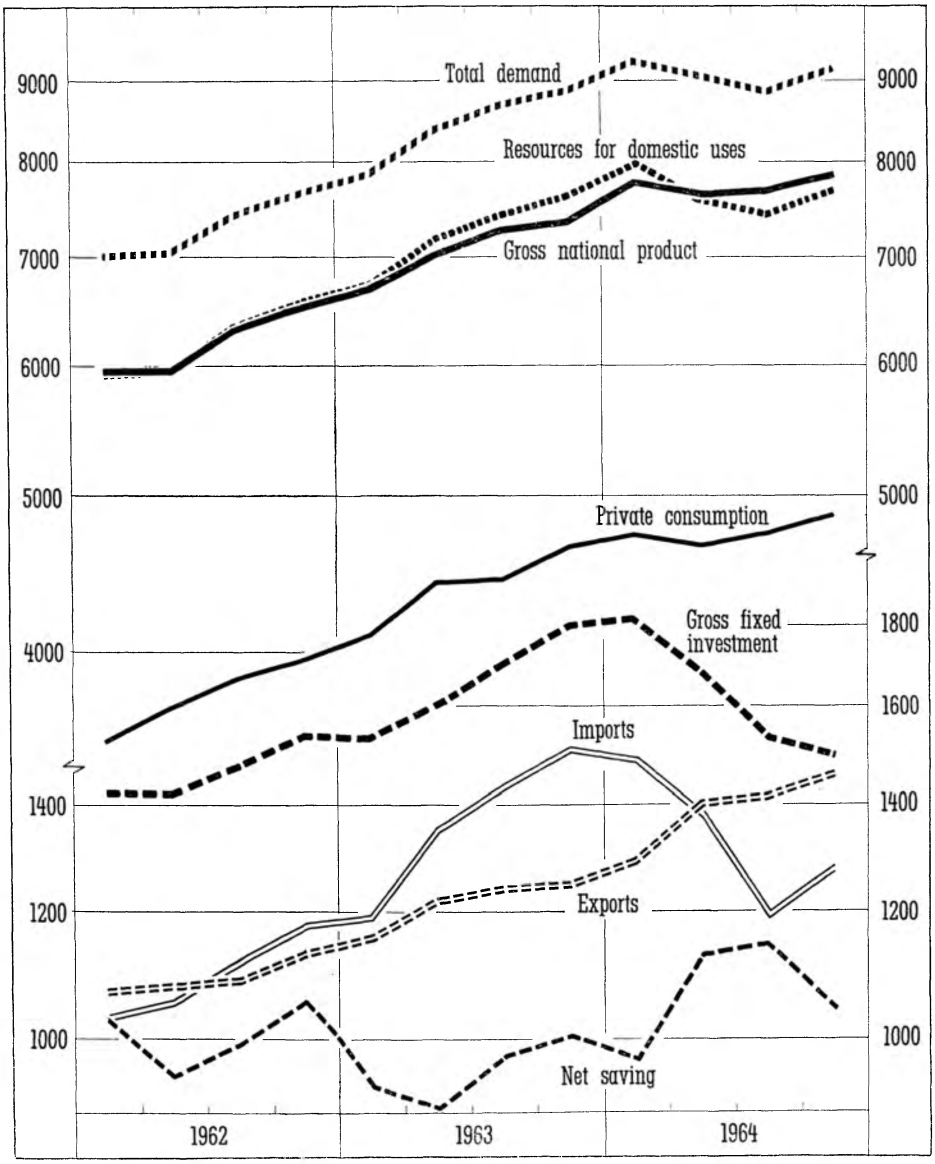
Gross Fixed Investment and Social Uses

Item	Value (billion current lire)		Percentage change in		
	1963	1964	volume	price	value
Gross fixed investment	*4,071*	*3,487*	— *19.2*	*6.1*	— *14.3*
of which:					
Agriculture	633	553	— 19.1	8.0	— 12.6
Industry	2,068	1,750	— 20.2	7.3	— 15.4
Transport and communications . .	871	651	— 27.3	2.8	— 25.3
Miscellaneous	499	533	— 1.0	7.9	6.8
Social Uses	*7,106*	*8,153*	*4.9*	*9.3*	*14.7*
of which:					
Public consumption	*4,536*	*5,115*	*3.9*	*8.6*	*12.8*
of which:					
Education	1,015	1,237	8.7	12.1	21.9
Public health	772	911	6.0	11.3	18.0
Defence	821	883	0.7	6.9	7.6
Others	1,928	2,084	1.9	6.1	8.1
Social investment	*2,570*	*3,038*	*6.7*	*10.8*	*18.2*
of which:					
Housing	1,884	2,197	5.0	11.0	16.6
Transport and telecommunications	442	545	12.9	9.2	23.3
Public works	172	211	8.1	13.5	22.7
Others	72	85	5.6	11.8	18.1
Total . . .	11,177	11,640	— 3.9	8.3	4.1

Source: Report on the Economic Situation in Italy.

Cyclical Developments.— Business conditions generally turned around sharply after the first quarter of the year, and this was clearly reflected in production and employment figures. Investment was the determining factor throughout. According to seasonally adjusted estimates, gross investment declined slightly during the first quarter of the year in comparison with the last few months of 1963, and then fell sharply during the second quarter and even more during the third. The contraction finally slowed down in the last quarter, when, however, gross investment at current prices was still about 20 per cent down on the corresponding figures of 1963 and 8 per cent on the 1964 average (Chart 1).

Chart 1



Total demand and supply and their components

(Seasonally adjusted quarterly estimates in billion current lire; logarithmic scale)

Building investment as a whole followed a similar pattern, though it still increased during the first quarter, only to decline later. In residential building fewer new constructions were begun. Consumption demand followed a much steadier course.

Seasonally adjusted imports of goods and services declined throughout the first three quarters of the year and then rose in the fourth; exports on the other hand surged ahead most of the year, except for the third quarter. As a result, the current deficit—still in seasonally adjusted figures—started diminishing rapidly during the first quarter and gave way to a small surplus during the second; the current account then remained first in large and later in decreasing surplus during the last six months of the year.

Resources for internal uses began by rising during the first quarter, then diminished for six months and increased again during the fourth quarter, when they were just a little more than during the corresponding period of 1963. Hower, given the intervening rise in prices, the real level of resources for domestic uses at the end of the year was appreciably below the end-1963 level.

Buoyant foreign demand could only partly offset the weakness of domestic demand, so that total demand contracted during the second and third quarters.

Incomes, Costs and Prices.— The country's total wage bill, including employers' contributions to the social security system, amounted to 14,580 billion lire in 1964, having risen by 1,562 billion over the 1963 figure of 13,018 billion. This increase of 12.0 per cent falls far short of the 22.8 per cent, or 2,421 billion, rise in 1963 (Table 5).

TABLE 5

Distribution of Income

(billion lire at current prices)

	1961	1962	1963	1964
Net national product at factor cost (1)	17,226	19,423	22,193	24,358
Increase	(1,534)	(2,197)	(2,770)	(2,165)
Percentage increase	*9.8*	*12.8*	*14.3*	*9.8*
Dependent labour incomes	9,006	10,597	13,018	14,580
Increase	(828)	(1,591)	(2,421)	(1,562)
Percentage increase	*10.1*	*17.7*	*22.8*	*12.0*
Other incomes (2)	8,220	8,826	9,175	9,778
Increase	(706)	(606)	(349)	(603)
Percentage increase	*9.4*	*7.4*	*4.0*	*6.6*

(1) According to OECD Schedule.
(2) Income from independent labour, profits, interest, rent, etc.
Source: Report on the Economic Situation in Italy.

Of last year's rise of 2,165 billion lire in net national product at factor cost, 72.1 per cent were absorbed by the 1,562 billion rise in dependent labour incomes, which in 1963 had taken up as much as 87.4 per cent of the total increment.

Other incomes, that is, independent labour incomes, profits, interest, rent, etc., rose together by 6.6 per cent, or 603 billion lire, from 9,175 to 9,778 billion. Since prices rose by about the same percentage, there was virtually no real increase at all. It follows that the real increment in national income went almost entirely to wage labour, whose income rose by about 6 per cent.

TABLE 6

Incomes, Costs and Prices

Items	Billion lire		Percentage change 1961-62		Billion lire 1963	Percentage change 1962-63		Billion lire 1964	Percentage change 1963-64		Aver. ann. (compound) percentage change 1961-64	
	1961	1962	Total	per unit of output		Total	per unit of output		Total	per unit of output	Total	per unit of output
Dependent labour incomes	9,006	10,597	*17.7*	*10.5*	13,018	*22.8*	*16.8*	14,580	*12.0*	*8.8*	*17.4*	*12.1*
Other incomes (gross domestic)	10,205	11,024	*8.0*	*1.4*	11,664	*5.8*	*0.7*	12,471	*6.9*	*3.9*	*7.0*	*2.0*
Gross domestic product at factor cost	19,211	21,621	*12.5*	*5.6*	24,682	*14.2*	*8.7*	27,051	*9.6*	*6.5*	*12.1*	*7.0*
Indirect taxes . .	2,724	3,064	*12.5*	*5.6*	3,538	*15.5*	*9.9*	3,758	*6.2*	*3.2*	*11.3*	*6.3*
Gross domestic product at market prices	21,935	24,685	*12.5*	*5.6*	28,220	*14,3*	*8.8*	30,809	*9.2*	*6.1*	*12.0*	*6.9*
Import prices . . .				*(1.0)*			*(3.3)*			*(—)*		*(1.4)*
Incidence of imports on the general price level				*— 0.9*			*— 1.5*			*— 0.1*		*— 0.9*
Total costs = general price level				*4.7*			*7.3*			*6.0*		*6.0*

Sources: Yearbook of the Central Statistical Institute and Report on the Economic Situation in Italy.

Note.— Percentage changes per unit of output indicate the extent to which annual increases in money incomes and indirect taxes exceeded the growth of gross national product in real terms, calculated on gross domestic product at (1954) market prices. Percentage variations in import prices are calculated on the price index relevant for imports of goods and services. Changes in the general level of costs and prices are the same as changes in the price index calculated as the difference between total disposable resources at current and at constant prices. The incidence of imports on the general price level allows for the weight of imports of goods and services in total disposable resources.

Table 6 shows how incomes, costs and prices moved since 1961. It will be seen that last year the level of prices, as calculated by the difference between gross domestic product at factor cost in current and in constant prices, rose by 6.5 per cent, whereas dependent labour incomes and other incomes, per unit of output, rose respectively by 8.8 and 3.9 per cent.

III. *Production and Prices*

Agricultural Production.— Agricultural production picked up again in 1964 after two almost stationary years, but adverse weather conditions made the final outturn less good than had been forecast earlier in the year.

In geographical terms, a distinct improvement in Northern and Central Italy was associated with poor harvests of the crops widely grown in the South.

The gross marketable product of agriculture, in quantitative terms, was 3.1 per cent higher in 1964 than the year before. The harvests of wheat and spring vegetables were much better, but the index for fruit crops was held back by a very poor olive harvest and rose only slightly. For the first time in three years there was an improvement in animal husbandry, where the stock of beef cattle has been increasing steadily since the end of 1963; livestock farmers also made a sustained effort to improve quality through selective breeding centres.

The increase in agricultural production in 1964 was associated with an appreciable easing of the strains to which the market had been subject in recent years. The total volume of food consumption rose by only 1.5 per cent, and meat consumption actually declined slightly.

Agricultural inputs as a whole increased by as much as gross marketable product, namely, by 3.1 per cent. Farmers used less fertilizers, but more pesticides, seeds, fodder, fuel and power, and about the same amount as before of other goods and services.

In terms of value, the gross marketable product of agriculture was worth 4,575 billion lire, a 6.4 per cent increase over the 1963 figure of 4,300 billion. The value of both field crops and animal products rose by about 9 per cent, that of fruit crops by only 0.8 per cent.

While the value of gross marketable product in Central and Northern Italy rose by some 10 per cent, it remained more or less at the preceding year's level in the South.

Industrial Production.— After expanding uninterruptedly, if unevenly, since the early postwar years, industrial production was stationary last year. The annual average index calculated by the Central Statistical Institute for industrial production (including seasonal industries but excluding building) rose by a mere 0.7 per cent from 235.4 to 237.0 (1953 = 100). In 1963 the corresponding rise had been 8.2 per cent, and the annual compound rate of growth over the period 1954-1963 was 8.9 per cent (Table 7).

Including building, with its rate of 3.7 per cent, overall industrial production increased by 1.0 per cent.

Poor as they are, these figures would be a good deal worse if the weakness of domestic demand had not been offset by a vigorous recovery of foreign demand, thanks in part to favourable world economic conditions and in part to the efforts of Italian producers, who were stung into action by the difficulties of selling their product at home.

A breakdown of the overall results by categories of use shows consumer durables (— 6.0 per cent) and capital goods (— 5.7 per cent) to have done worst. The only exception in this group was the production of building materials, where the high levels of activity of late 1963 continued into the early months of last year and pushed up the annual average to show an increase over 1963.

Engineering industries were hit most heavily (— 12.5 per cent), in spite of a further considerable rise in foreign sales.

The results recorded by companies making transport vehicles were not much better (— 9.8 per cent). Domestic sales of motor vehicles declined sharply, as indeed could be seen in the

Table 7

Annual Percentage Changes in the Indices of Industrial Production

Indices	1961	1962	1963	1964	Annual compound rate of growth			Index 1964 (1953=100)
					1954-63 10 years	1954-58 5 years	1959-63 5 years	
General index (incl. building)	9.5	9.3	8.2	1.0	8.9	7.5	10.3	236.9
General index (excl. building)	9.5	9.5	8.2	0.7	8.9	7.3	10.6	237.0
Producer goods	12.7	11.7	9.7	8.9	11.5	9.9	13.1	324.2
Capital goods (incl. building)	10.9	8.0	8.3	— 3.1	9.2	8.3	10.1	234.6
Capital goods (excl. building)	11.5	8.1	8.4	— 5.7	9.5	8.1	10.9	233.8
Consumer goods	4.8	8.6	6.6	0.2	6.3	4.8	8.0	184.9
Mining and quarrying	5.9	3.9	— 3.5	6.2	6.8	10.0	3.8	208.6
Manufacturing industry	9.8	— 0.1	19.4	0.3	9.1	7.3	10.9	239.9
Electricity and gas	6.6	6.8	9.3	5.2	7.2	5.9	8.5	209.9
Building	9.6	7.8	7.9	3.7	8.6	9.0	8.2	236.4
Manufacturing industry:								
Food	2.8	5.3	4.0	1.7	5.1	5.5	4.8	167.5
Tobacco	4.9	3.6	— 1.0	5.4	3.5	4.2	2.8	148.8
Textiles	— 0.6	6.9	3.7	— 6.7	3.4	0.9	5.9	130.2
cotton	*— 0.3*	*5.7*	*2.8*	*— 7.2*	*3.0*	*1.1*	*5.0*	*124.9*
wool	*— 3.1*	*8.5*	*— 2.6*	*— 8.7*	*2.3*	*— 0.3*	*4.9*	*114.0*
Hides and leather	10.4	1.5	6.7	— 6.7	5.8	4.2	7.4	163.9
Shoes and boots	8.1	0.8	8.1	— 3.8	6.3	6.3	6.4	178.0
Wood (excl. furniture)	10.3	4.0	— 0.8	— 1.0	4.6	2.9	6.4	155.8
Wooden furniture and fixtures	4.3	2.2	6.4	2.1	4.5	1.6	7.5	158.8
Paper	9.4	8.0	6.0	— 1.6	8.2	7.0	9.4	216.1
Rubber	10.5	— 0.8	20.9	— 2.4	8.6	3.1	13.7	223.4
Metallurgy	9.0	4.8	5.8	— 2.2	10.6	11.4	9.9	269.1
ferrous metals	*9.9*	*5.5*	*5.9*	*— 3.6*	*11.7*	*12.7*	*10.7*	*292.1*
non-ferrous metals	*0.7*	*— 2.7*	*5.0*	*13.1*	*3.3*	*3.5*	*3.0*	*156.6*
Engineering	15.3	3.7	9.1	— 12.5	7.9	5.1	10.7	187.0
machinery other than electrical	*12.3*	*1.6*	*10.7*	*— 11.6*	*6.8*	*4.2*	*9.6*	*172.1*
electrical machinery	*22.3*	*1.2*	*6.3*	*— 20.2*	*2.6*	*— 0.5*	*5.8*	*103.1*
precision instruments	*20.2*	*11.0*	*6.1*	*— 7.6*	*18.9*	*19.2*	*18.6*	*521.0*
Transport vehicles	12.2	17.5	18.0	— 9.8	13.5	11.3	15.7	320.7
Non-metallic minerals	8.6	17.8	5.9	6.1	11.0	9.8	11.9	300.9
cement	*12.6*	*11.8*	*9.6*	*3.4*	*10.9*	*9.9*	*11.5*	*291.6*
glass (sheets and plates)	*4.0*	*22.2*	*1.2*	*10.6*	*11.7*	*10.7*	*12.6*	*333.6*
Chemicals	15.8	14.3	8.4	9.1	13.8	12.0	15.7	397.2
Petroleum and coal derivatives	12.7	18.4	14.5	17.7	13.3	12.5	14.1	408.9
Man-made fibres	14.4	29.0	13.7	19.1	16.9	12.8	21.2	568.9

figures for new registrations, which were one quarter lower for motor cars and one third lower for industrial motor vehicles; however, Italian producers managed not only to sell more abroad, but also to increase their share of the domestic market.

Changes in foreign trade and their effect on domestic output were most clearly reflected in the steel industry. A combination of sharply increased foreign sales and a relatively smaller but absolutely larger fall in purchases abroad halved net imports of iron and steel products; in these circumstances, output contracted by only 3.6 per cent, whereas domestic demand is estimated to have shrunk by some 14 per cent.

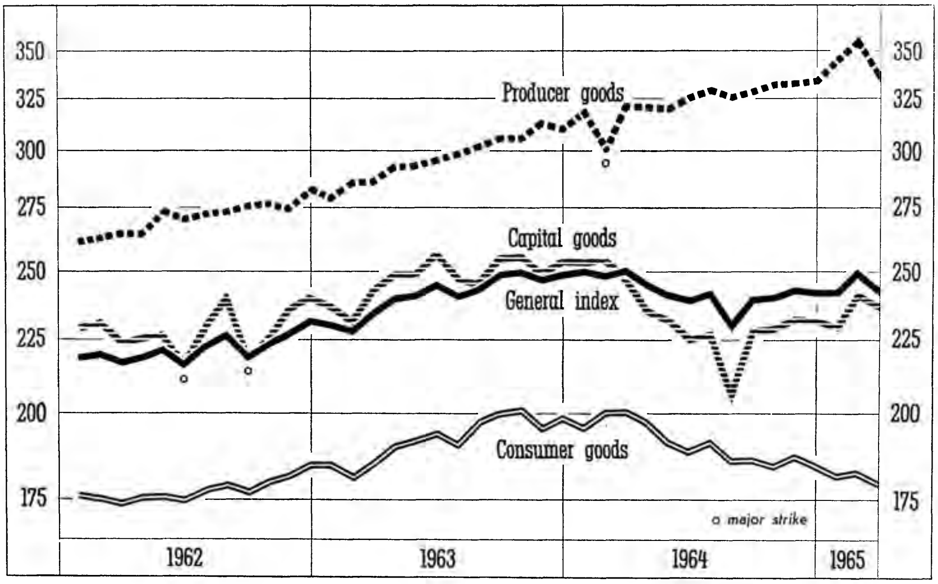
In consumer goods a fall in the production of durables was associated with rises of 1.1 and 2.0 per cent, respectively, in the production of semi-durables and non-durables. This disparity is a reflection of differences in the elasticity of demand with respect to spendable income. Taking all consumer goods together, output remained stationary.

A further, though moderate, rise in primary consumption helped food processing industries to expand their output. Larger exports failed to offset the decline of domestic demand for natural textiles, but man-made fibres did very well indeed, thanks to the industry's traditionally large export markets, its high efficiency and the growing substitution of man-made for natural fibres in consumption.

Unlike other industries, those producing fuel and power and producer goods raised their output by 8.9 per cent, which is almost as much as in 1963. This group includes the chemical industry, which again expanded its exports and scored new successes in the field of plastics and synthetic resins. The biggest increases were reported by oil refineries, which had to meet a rising domestic demand, on the part especially of motor vehicle users and thermo-electric power stations. These latter had to supply about 50 per cent more power last year, when poor rainfall conditions hampered the hydro-electric power stations, while demand especially for civilian uses and the electrochemical and electrometallurgical industries was rising. All told electricity production rose by 6.3 per cent.

Looking at the time path of industrial production in 1964 (Chart 2) it will be seen that stationary conditions around the turn of the year gave way to a decline at the end of the winter. Actually, some symptoms of difficulties, which do not show up in the general index, began to appear as early as the second half of 1963, when some major sectors, like steel and, a little later, engineering had to cut down production.

Chart 2



General index of industrial production
and indices of production of producer goods, capital goods and consumer goods
(1953 = 100; seasonally adjusted, logarithmic scale)

Early in 1964 the decline spread to the motor vehicles branch and to durable consumer goods generally. The rate of activity went down fairly fast in the capital goods industries (even though construction materials remained unaffected until May) and more slowly in the consumer goods industries.

The general index does not show the full extent of this fall, because it was boosted by the steady upward tendency of the producer goods industries which followed a course of their own throughout the year.

The trough came in the summer, especially with a plunge in August, when many engineering and transport vehicles firms extended their annual holiday period as an alternative to a further reduction of working time.

The autumn brought the first signs of scattered recovery, which significantly started in the same sector which had led the decline in 1963. It was, in fact, the steel industry which first showed a reversal of the downward tendency and then recorded high increases every month, which eventually pushed up the index for the whole group of capital goods industries. The reason was that big new steel mills came into operation at that time, and that others completed their extension and reorganization programmes.

Some signs of recovery appeared also in the motor vehicles industry, which benefited from the abolition of the taxes introduced in March. Together with the still rising output of producer goods industries, all this began to lift the general index of industrial production gently, even though activity in the consumer goods industries, and especially in textiles, still declined.

In the last quarter of 1964 the general index was still 2.8 per cent below its level of 12 months earlier. In detail, the indices for capital goods and for consumer goods stood, respectively, 8.6 and 6.6 per cent below, and the index for producer goods 7.3 per cent above, the corresponding 1963 levels.

At the close of the year, therefore, the industrial sector presented a rather uneven picture as regards variations in output levels with respect to the end of 1963, which are the resultant of divergent rates of growth or contraction during the year, and also as regards latest developments.

Results during the first few months of this year seem to confirm the signs of recovery visible during the last quarter of 1964. Generally speaking, it would appear that the industries to emerge from stagnation first are those which previously had invested most not only in plant extension, but also in rationalizing company structures to bring them into line with the requirements of new market situations. Improvements are seen, in fact, in chemicals, oil refining, steel and, to a lesser extent, in the motor vehicles industry; they are still slow to spread to other sectors, including such highly important ones as engineering and textiles.

Wholesale Prices.— The upward movement of wholesale prices, which began at the end of 1961 and speeded up considerably in 1963, became much less steep last year. The Central Statistical Institute's general index showed an annual average rise of 3.4 per cent, which was well below the 5.2 per cent of 1963 and hardly more than the 3.0 per cent of 1962. The deceleration is even more obvious in the end-year figures for twelve-month changes, which show rises of only 1.8 per cent for 1964 as against 5.5 per cent for 1963 and 4.6 per cent for 1962 (Table 8). Early this year the index declined gently, so that in March it stood only 1.0 per cent above its level of twelve months earlier.

The movements of the general index hide some rather striking disparities in its components. Agricultural prices remained stable in annual average terms, compared with a rise of 6.2 per cent in 1963; non-agricultural prices on the other hand increased on the average but not quite as much as in 1963 (4.3 and 4.8 per cent respectively).

In terms of twelve-month changes registered at the end of the year, agricultural prices followed a rise of 3.7 per cent in 1963 with one of only 0.7 per cent last year, which, moreover, was almost completely mopped up during the first quarter of the current year. Non-agricultural prices rose by 5.9 per cent over the course of 1963, by another 2.1 per cent up to December 1964, and then declined slightly during the first quarter of 1965.

The wholesale prices for agricultural products last year felt the influence not only of conditions at home, where favourable weather brought good harvests of most crops, but also of falling international prices after the conspicuous increases of 1963. As regards non-agricultural products, falling home demand failed to reverse the upward price trend in the face of the continuing cost push, which was by then in its third year; apart from that, rising world prices for industrial raw materials (+ 5 per cent, compared with + 3 per cent in 1963) pushed up the price of non-agricultural imports.

TABLE 8

Index of Domestic and International Wholesale Prices

(1953 = 100)

Index	1963	1964	1963 Dec.	1964		1965 March	Percentage change			
				March	Dec.		1964 / 1963	Dec. 63 / Dec. 62	Dec. 64 / Dec. 63	March 65 / March 64
a) DOMESTIC PRICES:										
Central Statistical Institute:										
General index	107.3	110.9	110.2	110.7	112.2	111.8	*3.4*	*5.5*	*1.8*	*1.0*
Foodstuffs	113.0	116.4	116.7	115.5	119.3	119.0	*3.0*	*6.1*	*2.2*	*3.0*
Industrial raw materials and manufactures (1)	103.4	107.1	105.7	107.4	107.3	106.9	*3.6*	*5.0*	*1.5*	— *0.5*
Industrial raw materials (1)	95.8	97.1	97.1	97.4	97.9	97.7	*1.4*	*3.0*	*0.8*	*0.3*
Manufactures	104.7	108.9	107.0	109.3	108.9	108.4	*4.0*	*4.9*	*1.8*	— *0.8*
Consumer goods	107.7	111.3	110.7	111.0	113.2	112.7	*3.3*	*5.4*	*2.3*	*1.5*
Capital goods	109.1	112.2	112.0	112.8	111.6	111.7	*2.8*	*5.8*	— *0.4*	— *1.0*
Producer goods	100.3	103.9	102.0	103.4	106.1	105.3	*3.6*	*4.4*	*4.0*	*1.8*
Chamber of Commerce, Milan:										
General index	101.8	105.7	104.8	105.2	107.3	105.2	*3.8*	*6.1*	*2.4*	—
Foodstuffs	110.0	112.8	114.0	111.4	114.8	111.2	*2.5*	*8.6*	*0.7*	— *0.2*
Industrial raw materials and manufactures	98.5	102.8	101.1	102.7	104.3	102.8	*4.4*	*5.1*	*3.2*	*0.1*
b) INTERNATIONAL PRICES:										
Volkswirt:										
General index	100.5	103.6	103.1	103.5	103.7	102.7	*3.1*	*5.7*	*0.6*	— *0.8*
Foodstuffs	95.7	96.3	99.9	99.3	94.1	93.0	*0.6*	*10.4*	— *5.8*	— *6.3*
Industrial raw materials	103.1	107.7	104.7	105.8	109.8	108.2	*4.5*	*3.1*	*4.9*	*2.3*

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(1) In our re-elaboration of the Central Statistical Institute's indices construction timber, lignite, crude petroleum and quarrying products are not included in the index of industrial raw materials, but are included in the combined index of industrial raw materials and manufactures.

Retail Prices and the Cost of Living.— Retail prices in their turn rose less (5.8 per cent) over the course of last year than they had done in 1962 (6.5 per cent) and in 1963 (6.9 per cent) (Table 9). Last year's almost identical figure of 5.9 per cent for the average annual rise in the general index of retail prices is about halfway between the 1962 (4.7 per cent) and 1963 (7.5 per cent) figures. Retail prices are seen to have risen strikingly more than wholesale prices.

The rise was fairly evenly spread as between food prices (+ 5.6 per cent) and the prices of other goods and of services (+ 6.0 per cent). In the latter group, services (+ 7.1 per cent) were well ahead of non-food prices (+ 4.1 per cent). Without services, the rise of retail prices over the course of 1964 would work out at only 5 per cent.

In March 1965 the retail price index stood 5.5 per cent above its level twelve months before. Contrary to what happened in earlier years, controlled rents did not go up in January 1965.

The new cost-of-living index (1961 = 100) followed the retail price index very closely, with a rise of 6.2 per cent over the course of 1964 only slightly exceeding the 5.8 per cent rise in retail prices (Table 9). The annual average increase compared with 1963 was 6.5 per cent; of the increment, 44 per cent are attributable to food (+ 5.3 per cent), 29 per cent to miscellaneous expenditure (+ 9.8 per cent), and the rest to other categories.

The new index being constructed on rather different principles, it does not lend itself readily to comparison with previous years. It may be worth recalling, though, that the old index, which was based on the reference year 1938, had risen by an annual average rate of 2.8 per cent between 1953 and 1961, and then climbed by 5.9 per cent in 1962 and by 8.8 per cent in 1963.

Like the other indices, the cost-of-living index too has been rising slightly less fast in the most recent months. The March 1965 figures show a twelve-month increase of 5.4 per cent, compared with 5.9 per cent up to March 1964.

TABLE 9

Index of Retail Prices and the Cost of Living

Index	1963	1964	1963 Dec.	1964		1965 March	Percentage change			
				March	Dec.		1964 / 1963	Dec. 63 / Dec. 62	Dec. 64 / Dec. 63	March 65 / March 64
Retail price index (1953 = 100)										
GENERAL INDEX	*132.5*	*140.3*	*136.2*	*137.8*	*144.1*	*145.4*	*5.9*	*6.9*	*5.8*	*5.5*
Food products	128.6	135.1	132.2	132.4	139.6	140.5	*5.1*	*6.8*	*5.6*	*6.1*
Non-food products and services	136.8	146.0	140.6	143.7	149.1	150.8	*6.7*	*7.1*	*6.0*	*4.9*
Textiles and related products	113.8	120.4	117.0	119.3	122.1	122.5	*5.8*	*6.1*	*4.4*	*2.7*
Electricity, gas and other fuels	106.0	111.5	108.8	110.7	113.6	114.1	*5.2*	*5.1*	*4.4*	*3.1*
Housing	265.6	286.1	270.3	280.6	290.7	294.7	*7.7*	*9.6*	*7.5*	*5.0*
Miscellaneous (1)	140.8	150.7	144.8	147.9	154.6	156.9	*7.0*	*7.2*	*6.8*	*6.1*
Cost-of-living index (1961 = 100) (2)										
GENERAL INDEX	*112.4*	*119.7*	*115.6*	*117.6*	*122.8*	*123.9*	*6.5*	*8.4*	*6.2*	*5.4*
Food	113.2	119.2	116.1	116.5	122.8	123.6	*5.3*	*7.5*	*5.8*	*6.1*
Clothing	110.5	116.8	113.7	115.8	118.7	119.4	*5.7*	*6.1*	*4.4*	*3.1*
Electricity and fuels	103.0	109.3	107.2	109.5	111.3	111.8	*6.1*	*7.4*	*3.8*	*2.1*
Housing	119.6	132.0	122.9	129.8	134.0	135.4	*10.4*	*14.1*	*9.0*	*4.3*
Miscellaneous expenditure	107.6	118.1	112.6	116.3	121.1	123.1	*9.8*	*9.4*	*7.5*	*5.8*

Source: Central Statistical Institute.

(1) Hygienic and medical articles; furniture and other household goods and appliances; private vehicles; domestic and similar services; transport, communications and public services; miscellaneous services (Bank of Italy's re-elaboration of Central Statistical Institute indices).

(2) This new index applies as of January 1946; the 1963 figures were obtained by modifying the January 1964 index according to the changes shown by the 1938 = 1 index. The percentage variations Dec. 63/Dec. 62 are those of the old 1938 = 1 index.

Wages.— The level of minimum contractual wages rose very unevenly last year in different sectors, and there was also a marked disparity between wages and salaries. Among wages properly speaking, only those in agriculture rose less (+ 11.7) than in 1963; elsewhere, the increase was larger, witness 17.3 per cent in industry, 14.4 per cent in trade and 18.7 per cent in transport (Table 10).

Salaries on the whole went up less than in 1963, except in trade, where the two years' figures are almost identical.

TABLE 10

Gross Wages (1)

(Index numbers, 1953 = 100)

Index	1963	1964	1963 Dec.	1964		1965 March	Percentage change			
				March	Dec.		1964 / 1963	Dec. 63 / Dec. 62	Dec. 64 / Dec. 63	March 65 / March 64
Minimum contractual rates (2)										
Wages:										
Agriculture	186.0	212.7	198.9	205.5	222.2	227.5	*14.4*	*17.6*	*11.7*	*10.7*
Industry	177.4	208.4	186.9	203.0	219.3	223.2	*17.5*	*15.3*	*17.3*	*10.0*
Trade	167.4	188.1	173.0	182.3	197.9	206.1	*12.4*	*13.4*	*14.4*	*13.1*
Transport	169.8	200.2	174.5	198.6	207.2	209.5	*17.9*	*8.0*	*18.7*	*5.5*
Salaries:										
Industry	187.5	213.9	196.7	207.8	223.9	227.4	*14.1*	*19.4*	*13.8*	*9.4*
Trade	179.2	204.5	185.8	196.4	216.9	224.2	*14.1*	*16.8*	*16.7*	*14.2*
Public administration	202.8	212.5	208.3	208.3	216.8	221.0	*4.8*	*25.0*	*4.1*	*6.1*
Actual earnings in industry (3)										
Average hourly earnings:										
Industry as a whole	200.2	224.1	215.6	219.3	240.0	—	*11.9*	*15.2*	*11.3*	—
Manufacturing industry	198.0	220.6	212.6	215.8	236.4	—	*11.4*	*13.9*	*11.2*	—
Food	202.4	251.0	250.1	252.2	280.3	—	*24.0*	*30.0*	*12.1*	—
Textiles	193.2	213.7	204.6	205.9	229.8	—	*10.6*	*11.7*	*12.3*	—
Metals and engineering . . .	192.3	210.2	201.7	206.2	222.2	—	*9.3*	*11.6*	*10.2*	—
Chemicals	195.8	225.8	213.2	217.6	244.8	—	*15.3*	*15.6*	*14.8*	—

(1) Excluding family allowances and fringe benefits.

(2) ISTAT original index (1938 = 1) converted to the base year 1953 = 100.

(3) Industries included in the census of the Ministry of Labour and Social Security (excl. mining and prospecting).

As before, some part of the increase in contractual rates was due to the renewal of agreements, and some part to the automatic mechanism of the sliding wage scale based on the cost of living. The bonus went up by altogether 10 points in 1964, as it did in 1963; of these 3 were last year for the period February-April, two for May-July, three for August-October, and another 2 for November-January. This year the sliding scale has so far gone up by two points in February and by another point in May.

Actual earnings in industry rose a little less last year than contractual rates. The index of average hourly earnings in industry, excluding family and other allowances, rose by 11.3 per cent over the course of last year, that is, less than in 1963; similarly last year's average annual rise of 11.9 per cent compares with 17.8 per cent in 1963 and with 15.1 per cent in 1962.

IV. *The Balance of Payments*

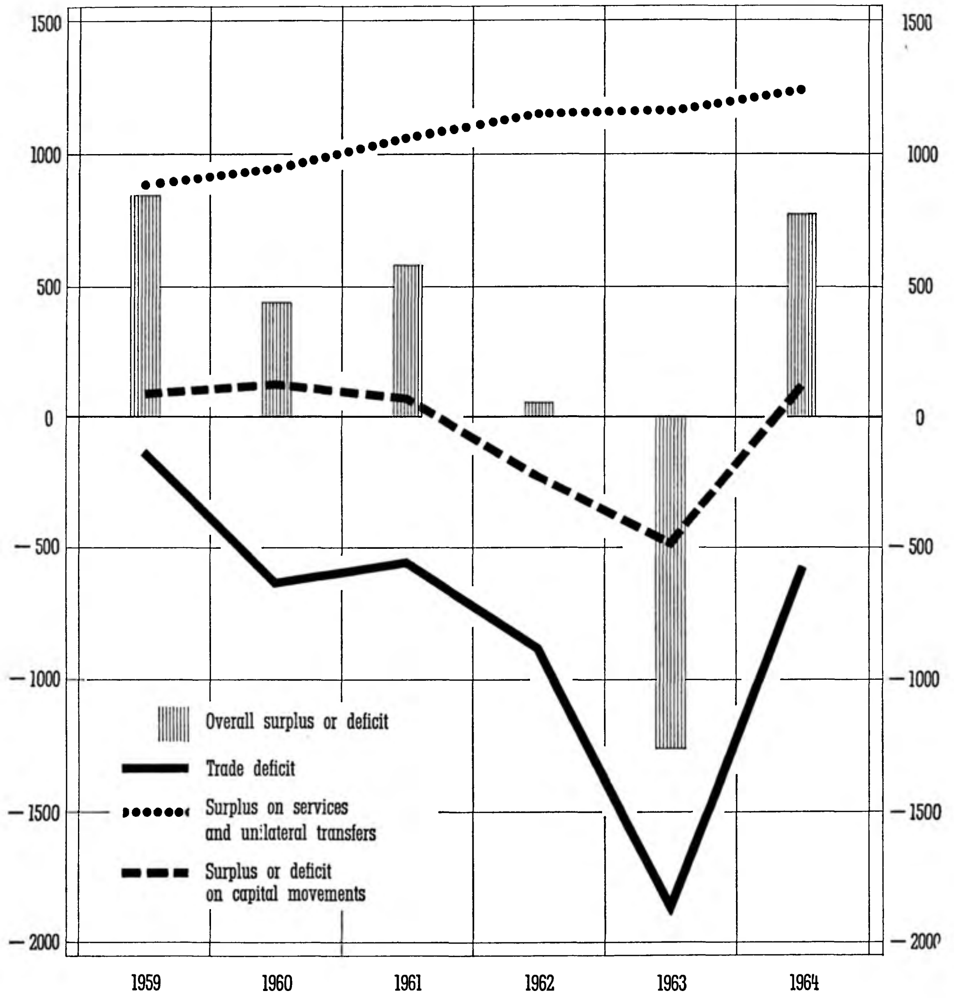
Italy's overall balance of payments closed last year with a surplus of 774 million dollars, the highest in five years (Chart 3). This followed a 1963 deficit of 1,252 million dollars.

The current account turned around from a deficit of 701 million dollars to a surplus of 695 million, and last year's net capital inflow of 93 million dollars followed a net outflow of 485 million in 1963. In both years the *Errors and omissions* item was negative, in the amount of 66 million in 1963 and 14 million last year (Table 11).

The trade balance, in fob values, was in deficit to the extent of only 568 million dollars, after the preceding year's 1,859 million; this spectacular improvement was the result of a 5.8 per cent drop in imports and a 17.9 expansion of exports.

The habitual surplus in the services and unilateral transfers accounts (including offshore procurements) rose from 1,158 to 1,263 million dollars; there was less to pay out on balance for freights and transport, tourist earnings rose and so did workers' earnings, but emigrants' remittances hardly changed.

CHART 3



The Italian balance of payments

(million dollars)

In the capital account (Table 12), net foreign investment in Italy is seen to have dropped sharply from 946 million dollars in 1963 to 550 million last year; net loans from abroad, on the other hand, increased from 286 to 522 million dollars. The diminution in the inflow of foreign investment is attributable entirely to investment in securities, and must be seen in conjunction with the steep fall in banknote repatriation from 1,470 to 577 million dollars; direct investment from abroad increased by more than 200 million dollars. The leads and lags as between the import

TABLE 11

Overall Balance of Payments (1)

(million dollars)

Items	Credit		Debit		Balance	
	1963	1964	1963	1964	1963	1964
1. Goods (fob)	4,983.7	5,876.0	6,842.5	6,443.5	−1,858.8	− 567.5
2. Services	2,717.5	2,971.8	1,895.1	2,029.0	822.4	942.8
3. Offshore procurements	50.4	58.7	—	—	50.4	58.7
4. Unilateral transfers	321.0	301.7	36.0	40.2	285.0	261.5
5. Total current items (1+2+3+4)	8,072.6	9,208.2	8,773.6	8,512.7	− 701.0	695.5
6. Capital Movements	1,517.6	1,220.5	2,003.0	1,127.7	− 485.4	92.8
7. Errors and omissions	—		65.4	14.4	− 65.4	− 14.4
8. Balance of payments (5 + 6 + 7)					−1,251.8	773.9
9. Monetary movements	1,663.3	773.2	411.5	1,547.1	1,251.8	− 773.9
9. 1 Central monetary institutions	960.2	663.2	358.2	994.8	602.0	− 331.6
9. 2 Other monetary institutions (banks)	703.1	110.0	53.3	552.3	649.8	− 442.3

(1) The figures, which have been approved by the Committee for the Balance of Payments, have been adjusted in the light of new statistics and estimates during the last two months and therefore differ in certain respects from the provisional figures of the *Report on the Economic Situation in Italy.*

and export of goods and the corresponding outgoing and incoming payments show that Italy last year extended a net total of 201 million dollars in trade credits to foreign countries; in 1963, conversely, Italy received a net 42 million of such credits.

TABLE 12

Capital Movements

(million dollars)

Items	Credit		Debit		Balance	
	1963	1964	1963	1964	1963	1964
1. Net investment abroad and from abroad	946.1	550.4	188.6	159.6	757.5	390.8
2. Net loans to and from abroad	285.6	522.3	56.4	10.1	229.2	512.2
3. Other long-term capital movements	27.5	—	66.8	61.8	− 39.3	− 61.8
4. Public capital movements	39.2	59.2	43.6	29.2	− 4.4	30.0
5. Total long-term capital movements (1 + 2 + 3 + 4)	1,298.4	1,131.9	355.4	260.7	943.0	871.2
6. Repatriation of Italian bank notes	—	—	1,470.4	577.1	−1,470.4	− 577.1
7. Short-term trade credits	219.2	88.6	177.2	289.9	42.0	− 201.3
8. Total capital movements (5 + 6 + 7)	1,517.6	1,220.5	2,003.0	1,127.7	− 485.4	92.8

As will be seen later (Table 23), 332 million dollars of the total balance-of-payments surplus went to increasing Italy's foreign reserves; the remaining 442 million were used by banks to reduce their indebtedness abroad.

The global balance-of-payments summary is shown in Table 13, according to the new internationally agreed schedule.

A breakdown of the various balance-of-payments items by geographical distribution (Table 14) shows that about half of last year's improvement in the current account was due to transactions with other members of the European Economic Community, and more especially to trade. Merchandise imports from other EEC countries contracted by a little more than the average (6 as against 5.8 per cent), but the export rise of 26.1 per cent was well ahead of the overall average rate of 17.9 per cent. Imports from the United States and other developed countries outside the EEC fell by much more than the average, and exports to them rose at a less-than-average rate. In absolute figures, the current account with EEC countries showed a surplus of 426 million dollars (a deficit of 217 million in 1963). There was also a net surplus of 357 million dollars in Italy's current transactions with the United States and other non-EEC developed countries (a deficit of 157 million in 1963), and a considerable improvement in the balance of capital transactions with them.

Italian merchandise imports from developing countries were a little more last year than in 1963, and exports to them increased by 16.6 per cent. Accordingly, the trade gap diminished less in relation to this group of countries than it did elsewhere. At the same time the surplus on services and unilateral transfers fell sharply, in marked contrast to these accounts with developed countries.

With exports to Sino-Soviet countries almost stationary, the entire reduction in the trade deficit with them is attributable to a fall in imports. A net capital outflow of 14 million dollars replaced the preceding year's net inflow of 26 million dollars.

Looking, finally, at the balance of payments from the point of view of its development over time (in seasonally adjusted figures), it will be seen that the steady deterioration of the balance

TABLE 13

Global Balance of Payments Summary

IMF-OECD schedule

(million dollars)

PART I

Item	Credit		Debit		Balance	
	1963	1964	1963	1964	1963	1964
A. Goods and Services	7,751.6	8,906.5	8,737.6	8,472.5	− 986.0	434.0
1. Merchandise (fob)	4,983.7	5,876.0	6,842.5	6,443.5	−1,858.8	− 567.5
2. Freight and insurance on international shipments	318.6	357.1	602.6	619.3	− 284.0	− 262.2
2. 1 Freight	311.8	350.6	594.0	611.2	− 282.2	− 260.6
2. 2 Insurance	6.8	6.5	8.6	8.1	− 1.8	− 1.6
3. Other transportation	370.0	391.9	258.2	279.0	111.8	112.9
3. 1 Passenger fares	191.5	204.9	38.7	40.2	152.8	164.7
3. 2 Other	178.5	187.0	219.5	238.8	− 41.0	− 51.8
4. Travel	931.6	1,035.4	182.8	208.7	748.8	826.7
5. Investment income	128.0	144.8	241.7	243.3	− 113.7	− 98.5
6. Government, not included elsewhere	141.2	124.0	92.7	72.5	48.5	51.5
6. 1 Military transactions	50.4	58.7	—	—	50.4	58.7
6. 2 Other transactions	90.8	65.3	92.7	72.5	− 1.9	− 7.2
7. Other services	878.5	977.3	517.1	606.2	361.4	371.1
7. 1 Workers' earnings	335.5	375.5	48.3	56.5	287.2	319.0
7. 2 Other	543.0	601.8	468.8	549.7	74.2	52.1
B. Transfer Payments	321.0	301.7	36.0	40.2	285.0	261.5
8. Private transfers	321.0	301.7	—	—	321.0	301.7
8. 1 Emigrants' remittances	282.9	280.0	—	—	282.9	280.0
8. 2 Other	38.1	21.7	—	—	38.1	21.7
9. Public transfers	—	—	36.0	40.2	− 36.0	− 40.2
9. 1 Reparations	—	—	10.0	7.6	− 10.0	− 7.6
9. 2 Other	—	—	26.0	32.6	− 26.0	− 32.6

TABLE 13

Global Balance of Payments Summary

IMF-OECD schedule

(million dollars)

PART II

Item	ASSETS						LIABILITIES					
	Credit		Debit		Balance		Credit		Debit		Balance	
	1963	1964	1963	1964	1963	1964	1963	1964	1963	1964	1963	1964
C. Capital and Monetary Gold	1,130.7	877.4	1,035.5	1,751.0	95.2	— 873.6	2,693.3	1,764.5	2,022.1	1,572.0	671.2	192.5
10. Private long-term (including all direct investment)	137.5	167.0	626.5	668.7	— 489.0	— 501.7	1,916.8	1,551.7	438.4	410.1	1,478.4	1,141.6
10. 1 Direct investment	56.4	51.9	214.7	204.3	— 158.3	— 152.4	384.5	566.5	54.7	31.8	329.8	534.7
10. 2 Other common stocks	10.3	8.5	46.7	22.6	— 36.4	— 14.1	876.4	223.0	273.3	219.8	603.1	3.2
10. 3 Other securities	12.7	8.3	6.6	1.4	6.1	6.9	39.5	30.5	26.3	18.0	13.2	12.5
10. 4 Loans	44.1	66.5	100.5	76.6	— 56.4	— 10.1	362.0	642.2	76.4	119.9	285.6	522.3
10. 5 Long-term trade credits	14.0	31.8	80.8	73.9	— 66.8	— 42.1	35.2	0.9	7.7	20.6	27.5	— 19.7
10. 6 Short-term trade credits	—	—	177.2	289.9	— 177.2	— 289.9	219.2	88.6	—	—	219.2	88.6
11. Repatriation of Italian bank notes	—	—	—	—	—	—	—	—	1,470.4	577.1	–1,470.4	— 577.1
12. Local government	—	—	—	—	—	—	19.1	23.3	—	—	19.1	23.3
13. Central government	25.9	44.4	69.5	73.6	— 43.6	— 29.2	61.4	82.3	41.3	46.4	20.1	35.9
13. 1 Long-term loans	25.9	44.4	66.0	70.1	— 40.1	— 25.7	61.4	82.3	41.3	46.4	20.1	35.9
13. 2 Other long-term assets and liabilities	—	—	3.5	3.5	— 3.5	— 3.5	—	—	—	—	—	—
14. Central monetary institutions	790.2	630.0	335.8	817.9	454.4	— 187.9	170.0	33.2	22.4	176.9	147.6	— 143.7
14. 1 Accounts with IMF	—	84.3	22.9	—	— 22.9	84.3	—	—	—	—	—	—
14. 2 Gold	—	236.5	99.7	—	— 99.7	236.5	—	—	—	—	—	—
14. 3 Other reserves	591.8	248.0	207.5	786.7	384.3	— 538.7	—	—	—	—	—	—
14. 4 Liabilities to official institutions	—	—	—	—	—	—	170.0	33.2	22.4	176.9	147.6	— 143.7
14. 5 Other foreign assets and liabilities	198.4	61.2	5.7	31.2	192.7	30.0	—	—	—	—	—	—
15. Other monetary institutions	177.1	36.0	3.7	190.8	173.4	— 154.8	526.0	74.0	49.6	361.5	476.4	— 287.5
15. 1 Foreign assets	177.1	36.0	3.7	190.8	173.4	— 154.8	—	—	—	—	—	—
15. 2 Foreign liabilities	—	—	—	—	—	—	526.0	74.0	49.6	361.5	476.4	— 287.5

TABLE 13

Global Balance of Payments Summary

IMF-OECD schedule

(million dollars)

PART III

Item	Credit		Debit		Balance	
	1963	1964	1963	1964	1963	1964
16. Goods and Services (1 through 7)	7,751.6	8,906.5	8,737.6	8,472.5	− 986.0	434.0
17. Transfer Payments (8 plus 9) . .	321.0	301.7	36.0	40.2	285.0	261.5
18. Foreign Assets and Monetary Gold (10 through 15, assets)	1,130.7	877.4	1,035.5	1,751.0	95.2	− 873.6
19. Foreign Liabilities (10 through 15, liabilities)	2,693.3	1,764.5	2,022.1	1,572.0	671.2	192.5
20. Total Net Transactions (16 through 19)	—	—	—	—	65.4	14.4
21. Net Errors and Omissions	—	—	—	—	− 65.4	− 14.4

on current account came to a halt in the first quarter of last year, and that the deficit gave way to a surplus again as of the second quarter (Chart 4). The decisive factor in this reversal of fortunes was the trade balance, with its increasing diminution of imports and export expansion. Italy imported 9 per cent less in the second quarter of last year than in the first, and in the third quarter 16 per cent less than in the second; during the same three-month periods, exports grew first by 11, and then by 4 per cent. The sharp contraction of the trade gap put the current account back into surplus during the second quarter of the year, for the first time since the beginning of 1963. Subsequently, the trade gap closed altogether and a surplus began to appear, which however dwindled to a mere 18 million dollars in the fourth quarter, when exports remained stationary and imports were again rising.

Early this year, the first quarter's imports were 2 per cent in excess of those of the last three months of 1964, but a 10 per cent increase in exports raised the trade surplus to 142 million dollars, and the whole current surplus to 487 million.

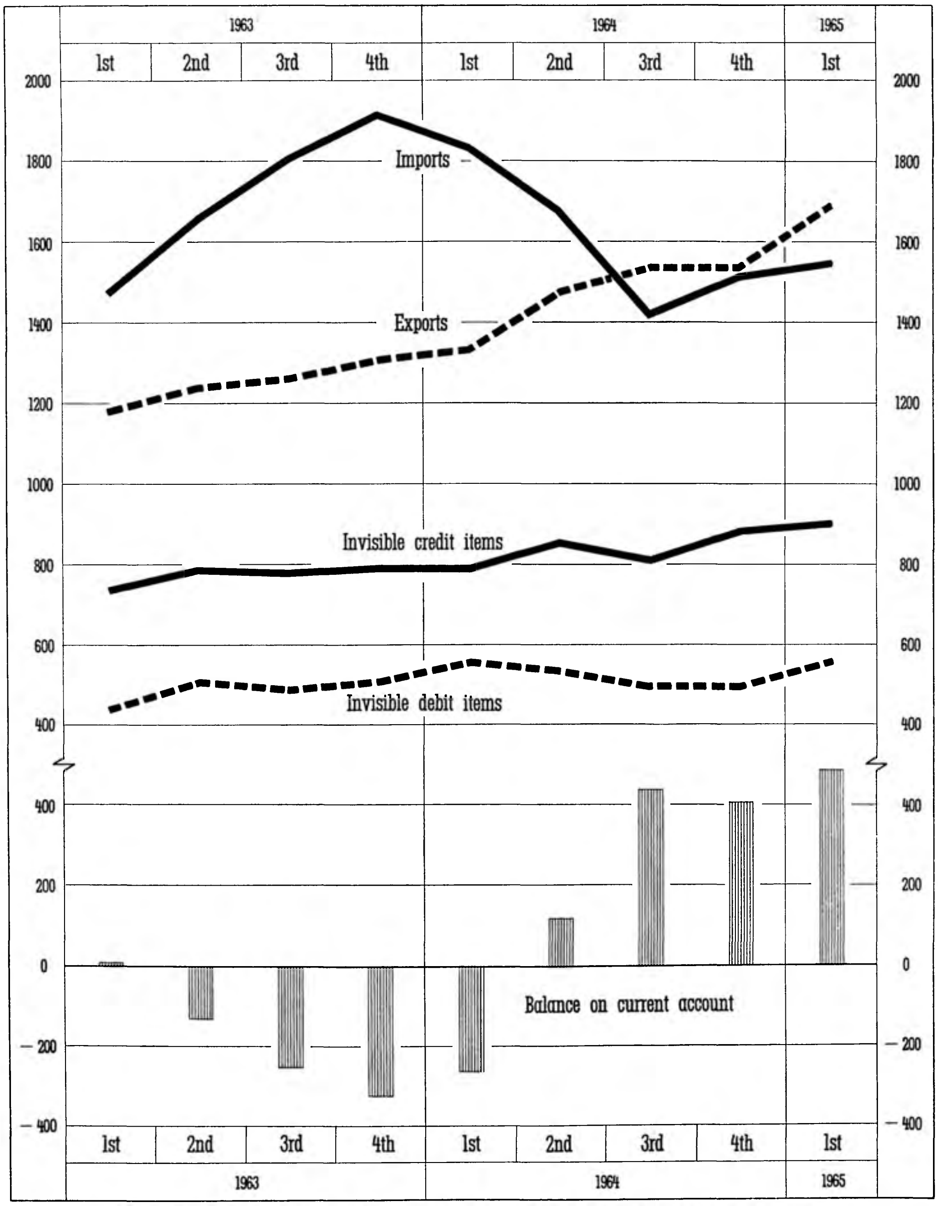
TABLE 14

Regional Balance-of-Payments Summary

(million dollars)

Items	Developed countries								Developing countries		Sino-Soviet area		International organizations and unallocated		Total	
	U. S.		EEC countries		Others		Total									
	1963	1964	1963	1964	1963	1964	1963	1964	1963	1964	1963	1964	1963	1964	1963	1964
Goods:																
Debit	920.5	837.5	2,402.1	2,257.3	1,527.7	1,377.9	4,850.3	4,472.7	1,636.0	1,656.9	351.1	307.5	5.1	6.4	6,842.5	6,443.5
Credit	477.0	507.2	1,801.7	2,272.6	1,179.0	1,362.3	3,457.7	4,142.1	1,214.4	1,414.6	292.0	296.0	19.6	23.3	4,983.7	5,876.0
Balance . . .	– 443.5	–330.3	–600.4	15.3	–348.7	– 15,6	–1,392.6	–330.6	–421.6	–242.3	–59.1	–11.5	14.5	16.9	–1,858.8	–567.5
Services:																
Debit	351.5	389.6	352.4	383.3	571.6	582.8	1,275.5	1,355.7	431.5	394.1	51.5	60.6	136.6	218.6	1,895.1	2,029.0
Credit	655.6	720.4	673.1	725.1	688.5	757.2	2,017.2	2,202.7	484.7	419.4	51.4	56.2	214.6	352.2	2,767.9	3,030.5
Balance . . .	304.1	330.8	320.7	341.8	116.9	174.4	741.7	847.0	53.2	25.3	– 0.1	– 4.4	78.0	133.6	872.8	1,001.5
Unilateral Transfers:																
Debit	—	—	—	—	—	—	—	—	24.8	20.7	2.1	2.0	9.1	17.5	36.0	40.2
Credit	122.7	104.5	63.0	68.6	91.1	93.5	276.8	266.6	44.1	30.7	0.1	—	—	4.4	321.0	301.7
Balance . . .	122.7	104.5	63.0	68.6	91.1	93.5	276.8	266.6	19.3	10.0	– 2.0	– 2.0	– 9.1	– 13.1	285.0	261.5
Current Account:																
Debit	1,272.0	1,227.1	2,754.5	2,640.6	2,099.3	1,960.7	6,125.8	5,828.4	2,092.3	2,071.7	404.7	370.1	150.8	242.5	8,773.6	8,512.7
Credit	1,255.3	1,332.1	2,537.8	3,066.3	1,958.6	2,213.0	5,751.7	6,611.4	1,743.2	1,864.7	343.5	352.2	234.2	379.9	8,072.6	9,208.2
Balance . . .	– 16.7	105.0	–216.7	425.7	–140.7	252.3	– 374.1	783.0	–349.1	–207.0	–61.2	–17.9	83.4	137.4	– 701.0	695.5
Capital Movements:																
Debit	130.9	175.4	119.5	157.8	1,870.5	858.9	2,120.9	1,192.1	301.4	245.6	4.7	18.1	219.1	320.1	2,646.1	1,775.9
Credit	303.5	512.2	225.2	436.6	1,244.6	632.8	1,773.3	1,581.6	128.7	106.6	30.3	4.2	228.4	176.3	2,160.7	1,868.7
Balance . . .	172.6	336.8	105.7	278.8	–625.9	–226.1	– 347.6	389.5	–172.7	–139.0	25.6	–13.9	9.3	–143.8	– 485.4	92.8
Monetary Movements:																
Debit	302.6	1,059.2	9.4	55.9	0.7	285.7	312.7	1,400.8	10.1	55.6	—	10.6	88.7	80.1	411.5	1,547.1
Credit	1,342.7	524.9	2.1	3.2	197.4	107.5	1,542.2	635.6	73.8	29.6	15.6	—	31.7	108.0	1,663.3	773.2
Balance . . .	1,040.1	–534.3	– 7,3	– 52.7	196.7	–178.2	1,229.5	–765.2	63.7	– 26.0	15.6	–10.6	–57.0	27.9	1,251.8	–773.9
Errors and omissions, multilateral settlements	–1,196.0	92.5	118.3	–651.8	569.9	152.0	– 507.8	–407.3	458.1	372.0	20.0	42.4	–35.7	– 21.5	– 65.4	– 14.4

CHART 4



Quarterly changes in the balance on trade and invisible account

(million dollars, seasonally adjusted)

Domestic and Foreign-Exchange Effects.— Exports are, in the Italian economic system, a most dynamic factor of income growth. During the three years 1959-1961 exports of goods and services, in value terms at 1954 prices, increased at an annual average rate of 17.3 per cent and absorbed a steadily growing share of the country's resources (13.9 per cent at the beginning and 17.1 per cent at the end of the period) (Table 15). Gross investment, at the same time, rose by 14 per cent, and consumption by 6.4 per cent. In this situation the country achieved a real rate of income growth of about 8 per cent, and its external surplus on goods and services account came to about 400 billion lire, at 1954 prices.

TABLE 15

Growth rates and composition of aggregate demand in Italy, 1959-64

Components of total demand	Percentage composition of total demand at the beginning of the period		Average annual percentage increase		Percentage composition of total demand at the end of the period	
	1954 prices	current prices	1954 prices	current prices	1954 prices	current prices
	Period 1959-61					
1. Consumption	67.4	68.7	6.4	7.3	61.8	63.9
2. Gross investment	18.7	18.4	14.0	14.7	21.1	20.9
3. Exports of goods and services	13.9	12.9	17.3	15.7	17.1	15.2
Total	100.0	100.0	—	—	100.0	100.0
	Period 1962-63					
1. Consumption	61.8	63.9	8.2	15.7	62.1	65.4
2. Gross investment	21.1	20.9	6.8	12.8	20.6	20.3
3. Exports of goods and services	17.1	15.2	8.5	11.4	17.3	14.3
Total	100.0	100.0	—	—	100.0	100.0
	Year 1964					
1. Consumption	62.1	65.4	2.6	8.9	63.0	66.3
2. Gross investment	20.6	20.3	−11.4	− 2.8	18.1	18.4
3. Exports of goods and services	17.3	14.3	11.0	14.7	18.9	15.3
Total	100.0	100.0	—	—	100.0	100.0

During the following two years, 1962-1963, major changes in income distribution caused private consumption to expand rapidly. The wages share in total income was some 60 per cent, compared with 55 per cent in the preceding three-year period; as a result, consumption, in real terms, rose by 8.2 per cent annually, the system's propensity to save declined and investment expanded by only 6.8 per cent annually, that is, at less than half the rate of the earlier three-year period. In their turn, exports grew much less vigorously than before. This shift in the relative rate of increase in demand factors slowed down real income growth to about 6 per cent a year and opened up

TABLE 16

Italy's Foreign Assets and Liabilities, 1963 and 1964

(end-year figures in million dollars)

Items	Assets		Liabilities		Balance	
	1963	1964	1963	1964	1963	1934
A. *Short-term*						
Public sector:						
Gold and convertible currency reserves	3,180.3	3,677.5	—	—	3,180.3	3,677.5
Other official assets and liabilities	429.0	149.7	214.6	70.9	214.4	78.8
Total . . .	3,609.3	3,827.2	214.6	70.9	3,394.7	3,756.3
Private sector:						
Commercial banks	1,283.8	1,438.6	2,538.2	2,250.7	− 1,254.4	− 812.1
Total short-term . . .	4,893.1	5,265.8	2,752.8	2,321.6	2,140.3	2,944.2
B. *Long-term*						
Public sector:						
Italian Exchange Office . . .	596.6	566.2	—	—	596.6	566.2
Bank of Italy	4.1	4.5	—	—	4.1	4.5
Loans	216.8	242.9	800.2	834.6	− 583.4	− 591.7
Italian government securities held abroad	—	—	5.2	4.4	− 5.2	− 4.4
Subscriptions to international organizations	112.7	116.2	—	—	112.7	116.2
Total . . .	930.2	929.8	805.4	839.0	124.8	90.8
Private sector:						
Loans	—	—	861.4	1,403.4	− 861.4	− 1,403.4
Investment	1,281.9	1,451.6	3,772.7	3,737.2	− 2,490.8	− 2,285.6
Trade credits	374.7	416.8	65.6	45.9	309.1	370.9
Total . . .	1,656.6	1,868.4	4,699.7	5,186.5	− 3,043.1	− 3,318.1
Total long-term . . .	2,586.8	2,798.2	5,505.1	6,025.5	− 2,918.3	− 3,227.3
Grand total (A + B) . . .	7,479.9	8,064.0	8,257.9	8,347.1	− 778.0	− 283.1

a yawning gap in the goods and services account, which meant a net import of foreign savings in the amount of close to 950 billion lire at 1954 prices.

The year 1964 saw the goods and services account get back into black again, with an 11 per cent export increase earning a surplus of some 30 billion (1954) lire. However, the situation was very different last year from what it had been in 1959-1961, for investment went down steeply by 11.4 per cent and consumption rose by a mere 2.6 per cent. The combined effect of the movements in exports, investment and consumption was that real income growth was limited to the modest rate of about 3 per cent.

As regards, finally, the foreign-exchange aspects of last year's balance-of-payments developments, the improvement is clearly reflected in the short-term position of official institutions (Table 16), while the long-term position of the public and the private sector together deteriorated by 309 million dollars.

Foreign investment outstanding in Italy at the end of last year was slightly less than 12 months earlier, in spite of new net, and mostly direct, foreign investment during the year. The reason for this apparent contradiction is that shares with a stock exchange quotation are valued at end-1964 prices, which, of course, were well below the previous year's levels.

All in all, such figures as are available suggest that at the end of last year Italy had an excess of 283 million dollars of foreign liabilities over foreign assets, which was 495 million less than at the end of 1963.

The Exchange of Goods and Services.— The value of Italy's imports at current prices diminished over the course of last year by 4.7 per cent, and her exports rose by 17.8 per cent. In absolute figures, imports fell from 4,744 billion lire in 1963 to 4,520 billion, and exports rose from 3,160 to 3,723 billion lire. Consequently, the trade deficit decreased from 1,584 to 797 billion, and the proportion of imports covered by exports rose from 67 to 82 per cent, its highest level since the exceptional peak of 1959 (Table 17).

TABLE 17

Value of Italy's Foreign Trade

(billion lire)

Year	Imports cif	Exports fob	Deficit	Export/Import ratio per cent
1957	2,296	1,594	702	69.4
1958	2,010	1,611	399	80.1
1959	2,105	1,821	284	86.5
1960	2,953	2,280	673	77.2
1961	3,265	2,614	651	80.1
1962	3,792	2,916	876	76.9
1963	4,744	3,160	1,584	66.6
1964	4,520	3,723	797	82.4

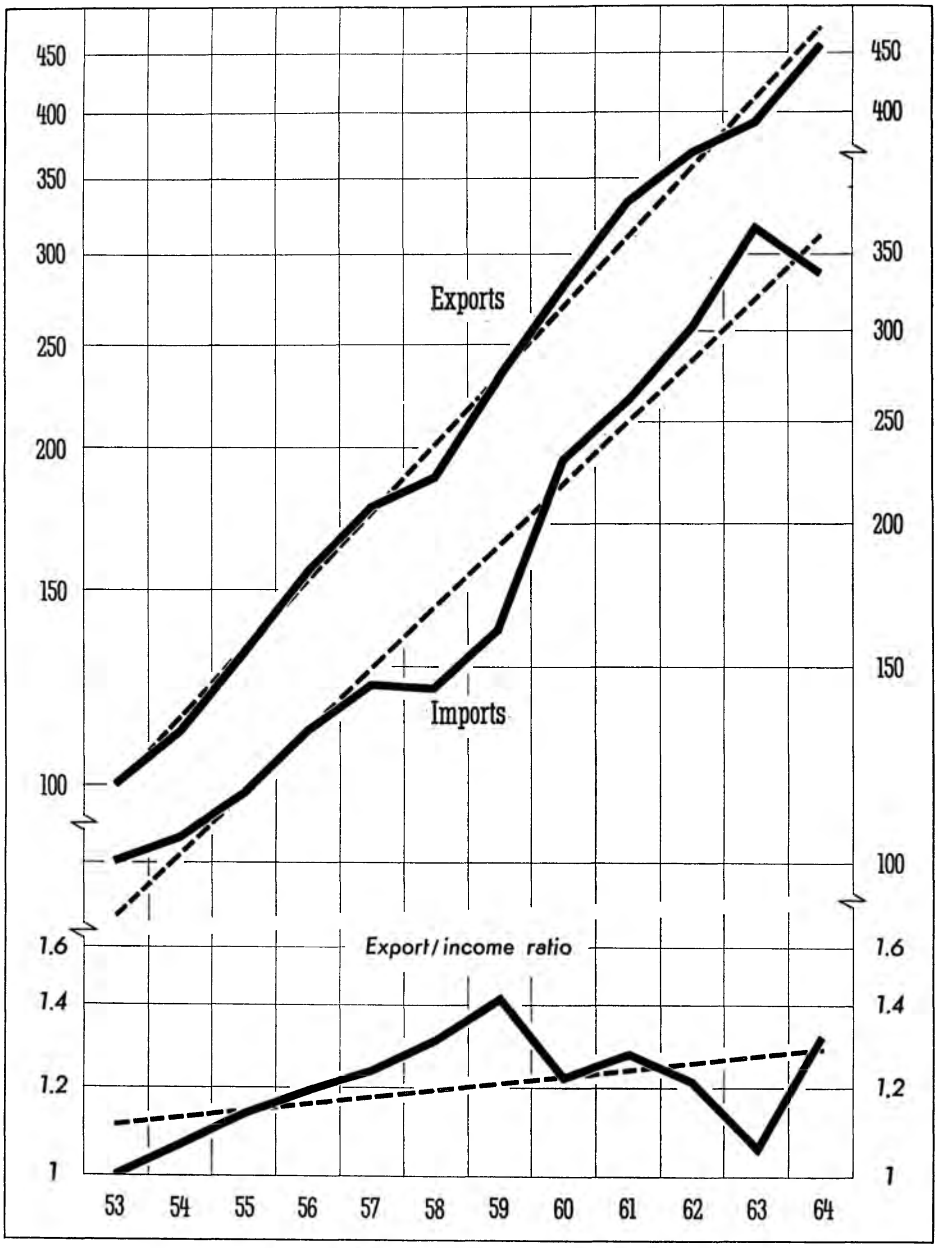
Source: Central Statistical Institute.

Indices calculated on the basis of the merchandise composition of foreign trade in 1963 show the cif prices of imports and the fob prices of exports to have risen last year by 1.3 and 0.6 per cent, respectively. It follows that in real terms imports contracted by 5.9 per cent and exports rose by 17.1 per cent.

As a result of the fall in the volume of imports, the respective index last year dipped slightly below the 12-year trend line (Chart 5), and thus returned to a more normal pattern after its excursion high above the trend line in 1963. The index of the volume of exports also returned to the trend line, and so foreign trade is back on its basic long-term pattern of exports growing relatively faster than imports.

Seasonally adjusted quarterly export figures for the last six years show a steady rise interrupted only once, during the last six months of 1960. The periods of steepest climb were June 1959–June 1960, and April–September 1964. As industrialization progresses in Italy and the country consolidates its place among the world's developed nations, the pattern of specialization works in the direction of increasing exports of manufactures. Last year, 70 per cent of these found a market in OECD countries, compared with 60 per cent in 1959. Italy's share in world trade in manufactures rose slowly from 5.7 per

CHART 5



Indices of the volume of foreign trade

(1953 = 100; logarithmic scale)

cent in 1961 to 6.4 per cent last year, when our exports of manufactures increased by 21 per cent—a figure which compares well with the corresponding 14 per cent increase for all other industrial countries together. However, it must be added that export markets were found at the cost of narrowing profit margins, since firms shifted only part of the increasing labour costs onto export prices (Table 18).

TABLE 18

Labour costs per unit of product in manufacturing industry: Indices for selected industrial countries, weighted by the countries' share in world exports of manufactures

(1958 = 100)

Countries	1962	1963	1964 (*p*)
Italy	99.2	109.4	115.0
Belgium, Federal Republic of Germany, France, Netherlands, Sweden, United Kingdom, Canada, United States, Japan	106.7	108.3	108.5
Index of Italian labour costs per cent of corresponding index in other countries	93.0	101.0	106.0

(*p*) Provisional figures.

Notes:

Calculations are based on figures for hourly earnings, production, employment and hours worked in manufacturing, as published in OECD, *General Statistics*, January 1965.

Figures for Japan are from United Nations, *Monthly Bulletin of Statistics*, March 1965. Figures for Italy are from the Central Statistical Institute's Monthly Bulletin of Statistics, and from the Labour Statistics of the Ministry of Labour and Social Security; they differ from those given elsewhere in this Report under the heading Economic Conditions in Italy, in so far as the latter figures refer only to a selected group of 24 manufacturing industries.

Production per man/hour was calculated by correcting industrial production figures for intervening changes in employment and hours worked. Labour costs per unit of product were obtained by dividing hourly earnings by production per man/hour.

In the case of France, Germany, Netherlands and Canada hourly earnings were deflated by a coefficient reflecting intervening variations in the exchange rate. Figures for man/hour production in Belgium, Netherlands and Sweden were not adjusted for changes in hours worked.

To get a single index of Italy's competitive position vis-à-vis other industrial countries, the figures for labour costs per unit of product were weighted by the separate countries' share in world trade in manufactures, calculated from figures given in *Board of Trade Journal*, 19 February 1965.

Total imports have been rising steeply since 1959, and especially in 1962 and 1963, when soaring purchases of consumer goods abroad pushed the curve well above its earlier levels. But this upward movement also owed much to a more evenly distributed increase in imports of capital goods and semimanufactures in connection with the progress of investment programmes. Last year, however, capital goods imports declined steadily, in contrast with others, which first contracted for nine months and then picked up again in the last quarter.

As regards the reasons for last year's foreign trade developments, the most striking feature is the effect of falling domestic demand upon imports (Table 19).

In private consumption, demand was held back not only by specific government measures to reduce foreign expenditure on less than strictly necessary goods, but more generally by the slow-down in the rate of expansion in labour incomes. Although food consumption was a little higher than in 1963, more abundant home supplies helped to contain food imports. Imports of capital goods and semimanufactures dropped for the very simple reason that demand was so weak as to leave a margin of excess supply at home.

Exports on the other hand benefited from the contraction of home demand, in so far as Italian producers had to step up their efforts to find markets abroad. World demand was buoyant, and a growing accumulation of stocks of finished products enabled exporters to quote shorter delivery dates. Lastly, expanding domestic demand in several of the major exporting countries eased the pressure of competition to the benefit of Italian products.

Last year's changes in the value of trade flows with separate countries or groups of countries are shown in Chart 6, by categories of merchandise.

The variations in these trade flows, and in their net balances, raise important questions in connection with the necessary volume of foreign exchange reserves. It seemed useful to measure foreign trade fluctuations in relation to gross national product at current prices. To this end the structural long-term upward trend was eliminated from the current import/income and export/income ratios, for separate cotegories of goods, as

Foreign

(billion

Items	1963			1964		
	Exports	Imports	Balance	Exports	Imports	Balance
						Merchandise
Raw materials	69.4	685.2	— 615.8	81.9	666.4	— 584.5
Producer goods	316.1	857.5	— 541.4	363.3	931.6	— 568.3
fuel and power	169.5	574.3	— 404.8	180.0	626.2	— 446.2
others	146.6	283.2	— 136.6	183.3	305.4	— 122.1
Semi-manufactures	390.2	816.7	— 426.5	525.9	713.5	— 187.6
Consumer goods	1,597.3	1,476.3	121.0	1,844.1	1,392.8	451.3
food	428.4	907.0	— 478.6	441.0	867.0	— 426.0
other non-durables	655.9	185.2	470.7	747.9	206.4	541.5
durables	513.0	384.1	128.9	655.2	319.4	335.8
Capital goods	786.6	907.9	— 121.3	907.5	815.3	92.2
plant, machinery and equipment	591.8	733.7	— 141.9	654.5	652.5	2.0
industrial motor vehicles	157.2	132.8	24.4	201.4	116.2	85.2
building materials	24.5	16.2	8.3	35.5	16.1	19.4
others	13.1	25.2	— 12.1	16.1	30.5	— 14.4
Total . . .	3,159.6	4,743.6	— 1,584.0	3,722.7	4,519.6	— 796.9
						Geographical
Developed countries	2,156.4	3,238.6	— 1,082.2	2,583.9	3,008.4	— 424.5
United States	298.1	651.4	— 353.3	317.0	612.2	— 295.2
EEC countries	1,120.8	1,564.1	— 443.3	1,416.2	1,477.9	— 61.7
United Kingdom, Iceland, Ireland	175.3	298.1	— 122.8	215.0	258.5	— 43.5
other OECD countries	486.3	551.3	— 65.0	533.2	483.1	50.1
other developed countries (1)	75.9	173.7	— 97.8	102.5	176.7	— 74.2
Developing countries	759.1	1,222.2	— 463.1	884.0	1,256.8	— 372.8
countries associated with the EEC	34.2	82.5	— 48.3	41.8	74.1	— 32.3
sterling area	154.9	296.8	— 141.9	188.5	370.9	— 182.4
other developing countries	570.0	842.9	— 272.9	653.7	811.8	— 158.1
Sino-Soviet-area	182.4	277.7	— 95.3	185.0	246.6	— 61.6
Unallocated	61.7	5.1	56.6	69.8	7.8	62.0
Total . . .	3,159.6	4,743.6	— 1,584.0	3,722.7	4,519.6	— 796.9

(1) Australia, Finland, New Zealand, Republic of South Africa.

TABLE 19

Trade

lire)

Annual change 1964				Composition per cent 1964		Items
Exports		Imports				
billion lire	*per cent*	billion lire	*per cent*	*Exports*	*Imports*	
composition						
12.5	*18.0*	— 18.8	— *2.7*	*2.2*	*14.7*	*Raw materials*
47.2	*14.9*	74.1	*8.6*	*9.8*	*20.7*	*Producer goods*
10.5	*6.2*	51.9	*9.0*	*4.9*	*13.9*	fuel and power
36.7	*25.0*	22.2	*7.8*	*4.9*	*6.8*	others
135.7	*34.8*	— 103.2	— *12.6*	*14.1*	*15.8*	*Semi-manufactures*
246.8	*15.5*	— 83.5	— *5.7*	*49.5*	*30.8*	*Consumer goods*
12.6	*2.9*	— 40.0	— *4.4*	*11.8*	*19.2*	food
92.0	*14.0*	21.2	*11.4*	*20.1*	*4.6*	other non-durables
142.2	*27.7*	— 64.7	— *16.8*	*17.6*	*7.0*	durables
120.9	*15.4*	— 92.6	— *10.2*	*24.4*	*18.0*	*Capital goods*
62.7	*10.6*	— 81.2	— *11.1*	*17.6*	*14.4*	plant, machinery and equipment
44.2	*28.1*	— 16.6	— *12.5*	*5.4*	*2.5*	industrial motor vehicles
11.0	*44.9*	— 0.1	— *0.6*	*1.0*	*0.4*	building materials
3.0	*22.9*	5.3	*21.0*	*0.4*	*0.7*	others
563.1	*17.8*	— 224.0	— *4.7*	*100.0*	*100.0*	Total
distribution						
427.5	*19.8*	— 230.2	— *7.1*	*69.4*	*66.5*	*Developed countries*
18.9	*6.3*	— 39.2	— *6.0*	*8.5*	*13.5*	United States
295.4	*26.4*	— 86.2	— *5.5*	*38.0*	*32.7*	EEC countries
39.7	*22.6*	— 39.6	— *13.3*	*5.8*	*5.7*	United Kingdom, Iceland, Ireland
46.9	*9.6*	— 68.2	— *12.4*	*14.3*	*10.7*	other OECD countries
26.6	*35.0*	3.0	*1.7*	*2.8*	*3.9*	other developed countries (1)
124.9	*16.5*	34.6	*2.8*	*23.7*	*27.8*	*Developing countries*
7.6	*22.2*	— 31.1	— *10.2*	*1.1*	*1.6*	countries associated with the EEC
33.6	*21.7*	— 8.4	*25.0*	*5.1*	*8.2*	sterling area
83.7	*14.7*	74.1	— *3.7*	*17.5*	*18.0*	other developing countries
2.6	*1.4*	— 31.1	— *11.2*	*5.0*	*5.5*	*Sino-Soviet area*
8.1	*13.1*	2.7	*52.9*	*1.9*	*0.2*	*Unallocated*
563.1	*17.8*	— 224.0	— *4.7*	*100.0*	*100.0*	Total

shown in Table 20. It will be seen that imports as a whole respond more to income changes than do exports (9.37 per cent as against 8.27 per cent), and this applies in detail also to the categories of raw materials (14.01 as against 13.79 per cent), capital goods (21.30 as against 15.79), and, most strikingly, consumer goods (13.40 as against 8.86). Only in the case of semimanufactures (12.18 as against 17.42) and producer goods (9.87 as against 12.87) are imports less responsive to income changes than exports.

TABLE 20

Current Import/Income and Export/Income ratios in Italy, 1950-1964

(per cent)

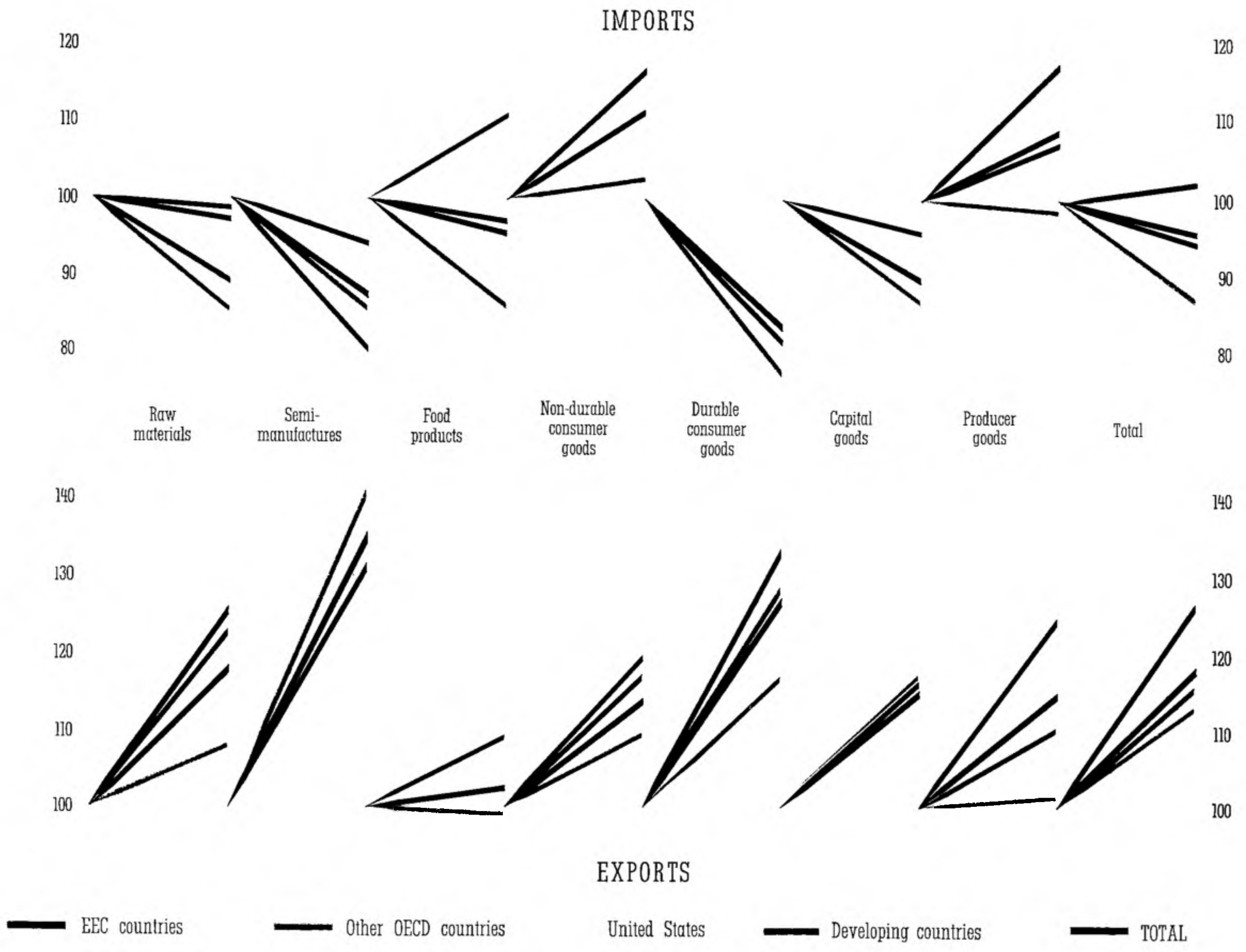
Item	Import/income ratio	Export/income ratio
Raw materials	14.01	13.79
Semimanufactures	12.18	17.42
Consumer goods	13.40	8.86
Capital goods	21.30	15.79
Producer goods	9.87	12.87
Total . . .	9.37	8.27

These results have to be taken with a grain of salt, of course, given the assumption of a linear tendency and also the influence of relative prices and world demand on the ratios. Nevertheless it does seem that imports, and especially imports of finished goods, are more flexible with respect to the domestic cycle, so that the Italian economy would now appear to be less vulnerable on the side of foreign trade than used to be thought. The main reason for this change to the better may well be that increased diversification in the structure of production enables imported goods to be more readily replaced by domestic supply, whereas wider markets and trade liberalization mitigate the fluctuations to which Italy's exports of non-essential goods are necessarily subject. Furthermore, the influences of expansion and recession in particular export markets tend to compensate each other in their effect on Italian exports, whereas Italian imports reflect more specifically only Italy's own cyclical developments.

CHART 6

INDEX NUMBERS OF ITALY'S FOREIGN TRADE, 1964

(1963 = 100)



Turning from trade to services, the balance on transport account closed last year with a deficit of 148 million dollars, compared with 170 million in 1963. Shipping rates were more favourable last year, and even though the tonnage of Italian imports increased, low average rates for liquid cargoes (which accounted for 55 per cent of imports) offset the effects both of the larger tonnage and of rising dry cargo rates.

Tourism brought in 11 per cent more than in 1963, with a total of 1,035 million dollars. Italians spent 209 million dollars on travelling abroad; the increase of 14 per cent was strikingly smaller than the preceding year's and came close to the 1960-1962 average. On balance, therefore, net foreign exchange earnings on this account amounted to 827 million dollars, as against 749 million in 1963.

Given that the number of nights spent by foreign tourists in Italy decreased by a further 3 per cent last year, the increase in foreign exchange earnings must be largely due to the intervening rise in prices.

Visitors from EEC countries accounted for 47 per cent of all foreign tourists in Italy last year (49 per cent in 1963); a heavy shortfall of German visitors (— 14 per cent) was not fully matched by an increased inflow of French ones. These two nations, together with Britons and Americans, accounted for more than three fifths of all foreign tourists.

The gross outward migratory flow from Italy is numbered at 278,000 persons, much the same as in 1963. Some 84 per cent of them travelled by their own means, and the rest were assisted, financially and otherwise, by national or international agencies. About 11 per cent more people went to Germany and 36 per cent more to Canada; on the other hand, 16 per cent fewer went to France, where expansion was slowing down, and 3 per cent fewer to Switzerland, which had introduced measures to break the boom.

Capital Movements.— Italy's external capital account, which had been in heavy deficit since the first quarter of 1962, and in 1963 to the extent of 485 million dollars, last year closed with a surplus of 93 million dollars. The determining factors in this improvement were direct investment, medium- and long-term foreign loans, and the sharp decrease in banknote repatriation (Table 21).

TABLE 21

Capital Movements in the Italian Balance of Payments (1)

(quarterly balances in million dollars)

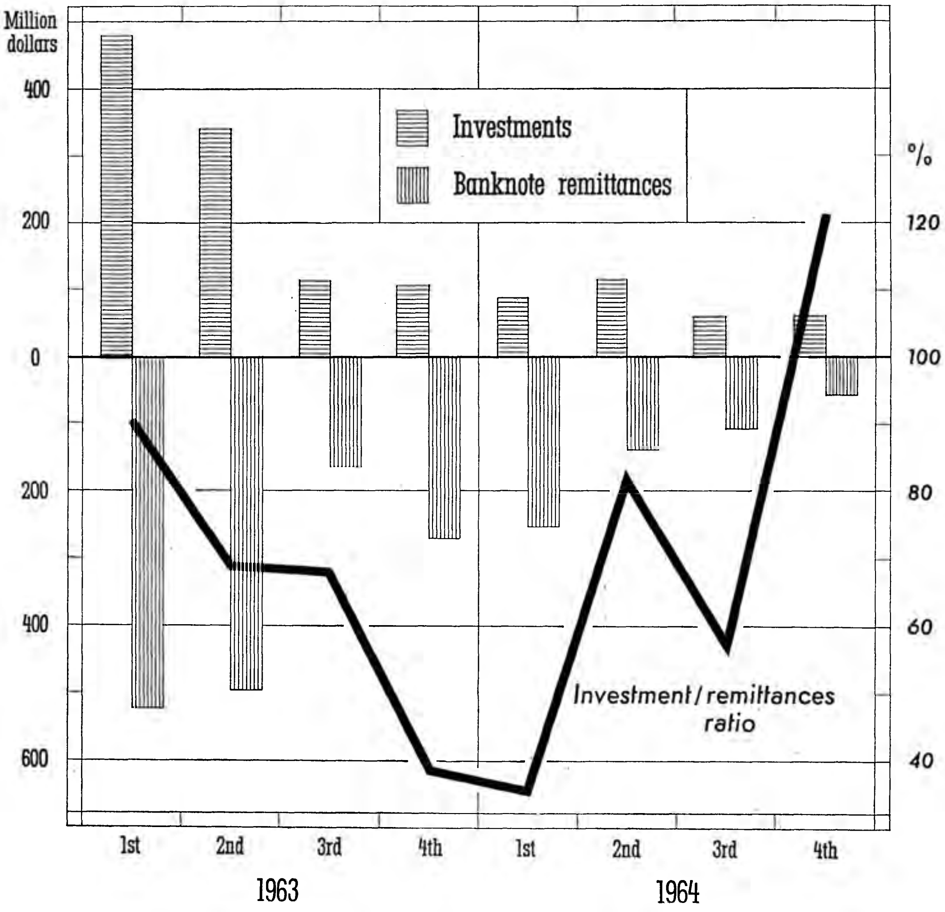
Items	1963					1964				
	1st	2nd	3rd	4th	Year	1st	2nd	3rd	4th	Year
1. Investment from abroad	480	309	113	44	946	128	264	92	67	551
2. Investment abroad .	– 19	– 60	– 40	– 70	– 189	– 17	– 15	– 77	– 50	–159
3. Private loans from abroad	25	90	54	117	286	88	162	142	131	523
4. Private loans to abroad	– 22	– 2	– 33	1	– 56	– 4	– 18	20	– 8	– 10
5. Public loans from abroad	1	—	1	19	21	—	– 10	18	28	36
6. Public loans to abroad	– 13	12	– 31	– 9	– 41	– 21	– 22	21	– 4	– 26
7. Local government . .	—	—	19	—	19	—	—	—	23	23
8. Trade credits from abroad	8	9	7	4	28	3	9	– 12	– 20	– 20
9. Trade credits to abroad	—	– 26	– 14	– 27	– 67	– 5	– 35	– 13	11	– 42
10. Other capital movements	—	—	—	– 4	– 4	—	—	—	– 4	– 4
11. Total long-term capital (1 through 10) .	460	332	76	75	943	172	335	191	173	871
12. Repatriation of Italian banknotes	– 525	– 499	– 168	– 278	–1,470	–261	–142	–114	– 60	–577
13. Short-term trade credits from abroad	– 40	– 15	– 42	– 80	– 177	– 47	– 83	– 57	–103	89
14. Short-term trade credits to abroad . .	32	45	89	53	219	128	156	–105	– 90	–290
15. Total capital movements (11 through 14)	– 73	– 137	– 45	– 230	– 485	– 8	266	– 85	– 80	93

(1) The (implied) + sign indicates a capital inflow from abroad, the — sign a capital outflow towards abroad.

Clandestine capital exports in the form of Italian banknotes sent abroad dropped sharply (from 1,470 million dollars in 1963 to 577 million last year) in consequence of certain concessions on the withholding tax on dividends and the generally brighter prospects of the lira. The contraction began in December 1963 and continued through 1964, most markedly in the second and fourth quarters.

Repatriated banknotes (which are, as such, recorded in the balance of payments as a capital outflow), were used largely abroad during the first quarter of the year; in the second, far fewer of them came in and the amount invested abroad was also much smaller; this latter rose again in the third quarter, but not to the levels of the first few months, and in the last quarter, finally, dropped sharply. For the first time since 1962, Swiss investment in Italy exceeded the amount of banknote repatriation from Switzerland during the last three months of 1964 (Chart 7).

Chart 7



Investments and banknote remittances originating in Switzerland and Liechtenstein
(quarterly figures in million dollars)

Foreign investment in Italy was nearly 500 million dollars less last year than in 1963 (820 as against 1,300 million), owing entirely to a drop in portfolio investments. Direct investment, on the contrary, rose appreciably (Table 22), mainly because foreign firms either increased the capital of their Italian subsidiaries or else took an equity stake in Italian companies. Outstanding examples of the first type of operation are the capital increases of *Shell Italiana* from 22 to 129 billion lire, and of *Esso Italiana*, which converted a 10-billion lire loan into equity capital. As regards equity participation agreements, *Dow Chemical* put 20 million dollars into *Ledoga*, and *3M* 30 million dollars into *Ferrania*. These four operations alone accounted for 237 million dollars of direct foreign investment.

The capital increase of *Shell Italiana* took the form of a subscription to 50 per cent of the equity of *Monteshell Petrolchimica* and the construction of a refinery at Taranto. In Italian statistics on capital movements the foreign exchange involved figures as coming from the Netherlands, but actually the funds originated in the United Kingdom.

The industrial branches most favoured by foreign investors were, in descending order of the magnitude of the funds involved, mineral oils (241 million dollars), chemicals (76 million) engineering (62 million) and residential building (58 million). Strikingly less than in 1963 went into hotels, raw materials and rubber.

As regards the source of the investment funds, considerably more came last year from the United States, the Netherlands and other EEC countries. Part of the inflow of foreign exchange into Italy was used to repay short-term bank credits. Swiss investment dropped from 233 million dollars in 1963 to 164 million last year.

Foreign investment in Italian securities began to contract late in 1963 and dropped throughout the whole of last year, reaching a total of only 223 million dollars as compared with 876 million in 1963. One major contributing factor in this development was that Italians exported far fewer banknotes, and to this extent the drop was apparent rather than real. Nevertheless, genuine foreign-held security investments also declined; those originating elsewhere than in Switzerland and Liechtenstein fell from 87 to 66 million dollars (Table 22).

TABLE 22

Foreign Investment and Banknote Remittances

(million dollars)

Countries	1962			1963			1964		
	Receipts	Payments	Balance	Receipts	Payments	Balance	Receipts	Payments	Balance
A. *Direct investment:*									
1. EEC countries	47.7	13.9	33.8	42.8	3.5	39.3	238.5	4.5	234.0
2. Switzerland and Liechtenstein	268.0	6.4	261.6	233.0	31.9	201.1	163.8	17.1	146.7
3. United Kingdom	15.7	0.5	15.2	17.6	0.3	17.3	20.6	7.3	13.3
4. United States	30.8	1.2	29.6	66.3	17.1	49.2	128.9	2.4	126.5
5. Other countries	16.7	1.7	15.0	24.8	1.9	22.9	14.7	0.5	14.2
Total . . .	378.9	23.7	355.2	384.5	54.7	329.8	566.5	31.8	534.7
B. *Portfolio investment:*									
1. EEC countries	31.0	34.7	— 3.7	48.4	28.6	19.8	41.9	31.3	10.6
2. Switzerland and Liechtenstein	582.7	165.4	417.3	789.5	203.0	586.5	156.5	159.6	— 3.1
3. United Kingdom	14.5	25.9	— 11.4	12.4	15.3	— 2.9	9.0	8.2	0.8
4. United States	19.1	24.9	— 5.8	10.5	21.2	— 10.7	9.9	7.9	2.0
5. Other countries	9.9	5.1	4.8	15.6	5.2	10.4	5.7	12.8	— 7.1
Total . . .	657.2	256.0	401.2	876.4	273.3	603.1	223.0	219.8	3.2
C. *Other investment:*									
1. EEC countries	7.6	1.1	6.5	7.3	3.6	3.7	7.1	2.8	4.3
2. Switzerland and Liechtenstein	13.6	1.6	12.0	23.4	9.6	13.8	13.5	3.1	10.4
3. United Kingdom	0.5	0.8	— 0.3	1.2	1.0	0.2	1.7	1.0	0.7
4. United States	1.1	3.6	— 2.5	1.9	7.2	— 5.3	1.5	5.5	— 4.0
5. Other countries	4.2	3.2	1.0	5.7	4.9	0.8	6.7	5.6	1.1
Total . . .	27.0	10.3	16.7	39.5	26.3	13.2	30.5	18.0	12.5
D. *Total investment:*									
1. EEC countries	86.3	49.7	36.6	98.5	35.7	62.8	287.5	38.6	248.9
2. Switzerland and Liechtenstein	864.3	173.4	690.9	1,045.9	244.5	801.4	333.8	179.8	154.0
3. United Kingdom	30.7	27.2	3.5	31.2	16.6	14.6	31.3	16.5	14.8
4. United States	51.0	29.7	21.3	78.7	45.5	33.2	140.3	15.8	124.5
5. Other countries	30.8	10.0	20.8	46.1	12.0	34.1	27.1	18.9	8.2
Total (A + B + C) . . .	1,063.1	290.0	773.1	1,300.4	354.3	946.1	820.0	269.6	550.4
E. *Banknote remittances:*									
1. EEC countries	—	1.0	— 1.0	—	2.1	— 2.1	—	3.2	— 3.2
2. Switzerland and Liechtenstein	—	761.9	— 761.9	—	1,456.0	— 1,456.0	—	556.9	— 556.9
3. United Kingdom	—	—	—	—	0.7	— 0.7	—	0.6	— 0.6
4. United States	—	—	—	—	—	—	—	0.5	— 0.5
5. Other countries	—	3.0	— 3.0	—	11.6	— 11.6	—	15.9	— 15.9
Total . . .	—	765.9	— 765.9	—	1,470.4	— 1,470.4	—	577.1	— 577.1

Portfolio disinvestment, though less than in 1963 (220 as against 273 million dollars) was still high. Analysis of the currencies involved suggests that a large part of this disinvestment is attributable to Italians selling securities previously acquired under a foreign name (with funds from non-resident capital accounts).

Italian investment abroad diminished last year by 40 million dollars from 268 to 228 million. The contraction occurred almost entirely in investments not involving foreign exchange transfers, and among them more especially portfolio investments, which dropped from 32 to 8 million dollars. There was a marked increase from 27 to 87 million dollars in Italian investment in the United States; by contrast, less went to the United Kingdom, the countries of the European Economic Community and developing countries.

Foreign medium- and long-term credits in the form of security issues abroad, direct loans to companies and loans to finance institutes amounted to 642 million dollars last year, compared with 362 million in 1963. Another 100 million dollars were borrowed by banks on the medium term (47 million in 1963), and these figure under bank indebtedness abroad.

Prominent among lenders were the United States (358 million dollars), Switzerland (156 million), and the United Kingdom (65 million); the biggest borrowers of new money were the iron and steel industry (199 million dollars), engineering companies (86 million) and special credit institutes (115 million). The chemical industry, on the other hand, while still making fairly large claims on foreign loan capital, took up less than in 1963.

Interest rates followed the general tendency on world money and capital markets and were lower in the first than in the second half of the year.

Foreign loans from public sources were also higher last year than in 1963 (106 as against 80 million dollars), thanks largely to loans conceded to the Cassa per il Mezzogiorno by the European Investment Bank and the European Coal and Steel Community. Not very much was drawn in the course of the year on the medium-term credit lines opened to Italy in March 1954 by the Export-Import Bank (200 million dollars) and the Commodity Credit Corporation (250 million). The International Bank for Reconstruction and Development recently approved a 100 million dollar loan to the Cassa per il Mezzogiorno, and these funds ought to become available in the course of the current year.

Repayments of private and public debts to foreign lenders also increased last year, but fell short, both in absolute and in relative terms, of new borrowing, so that the net capital inflow on this score (excluding medium-term bank credits) worked out at 581 million dollars, compared with 325 million in 1963. This year repayments, especially of private debts, are likely to be higher, given that part of the medium-term loans taken up in 1963 and 1964 fall due in the course of the year.

Private credits extended by Italians to foreign borrowers diminished by 24 million dollars in comparison with 1963, while corresponding repayments rose from 44 to 66 million. Public credits to abroad followed a similar pattern, with new loans net of repayments falling 14 million dollars short of the 1963 figure.

Short-term trade credits, as reflected in the leads and lags between the customs and the foreign-exchange statistics of foreign trade, showed pronounced and at times rather wide fluctuations, especially on the import side. On balance, a net inflow of 42 million dollars in 1963 turned into a net outflow of 201 million dollars last year (Table 21).

V. *Monetary Movements, Reserves and the Exchange Rate*

Of last year's balance-of-payments surplus of 774 million dollars, 442 million were used to reduce the Italian banking system's indebtedness abroad and the balance of 332 million went to increase official reserves in the form of gold and foreign exchange, second-line reserves and other medium- and long-term official assets abroad (Table 23). By the end of 1964 the net official reserves of the Bank of Italy and the Italian Exchange Office stood at 3,756 million dollars (362 million up on December 1963), and other medium- and long-term assets at 571 million

TABLE 23

Monetary Movements

(million dollars)

Movements reflected in the balance sheet of the	1963	1964
1) Bank of Italy:		
Gold and convertible currencies	— 434.6	497.2
Other net official reserves	25.3	— 135.6
Medium- and long-term assets	— 192.7	— 30.0
Total . . .	— 602.0	331.6
(billion lire, incl. leads and lags)	— *374.5*	*207.5*
2) Banking system:		
Net bank liabilities abroad	— 649.8	442.3
(billion lire)	— *406.1*	*276.4*
Total 1) + 2) . . .	— 1,251.8	773.9

The (implied) + sign indicates an increase in assets or decrease in liabilities, the — sign a decrease in assets or increase in liabilities.

(down 30 million on December 1963). The net debit position of Italian banks vis-à-vis abroad dropped over the course of the year from 1,254 to 812 million dollars (Table 24).

Italian banks which, in 1963, had attenuated the deflationary effects of the balance-of-payments deficit through borrowing abroad, last year absorbed in foreign repayments about three-fifths of the liquidity increment generated by the balance-of-payments surplus. The restrictions introduced in September and December 1963 on bank indebtedness abroad were followed in July 1964 by new instructions to the effect that banks were not to increase the net balance of their foreign debts beyond the level of 15 or 30 June, whichever was the lower.

The amount of open forward dollar positions between the banks and the Italian Exchange Office remained virtually unchanged throughout the first nine months of the year, subsequently increased slightly and reached high levels during the first quarter of 1965. During the six months following last September

TABLE 24

Net Foreign Position of the Italian Exchange Office, the Bank of Italy and Italian Banks

(End-month figures in million dollars)

Items	1963		1964				1965
	August	December	March	June	September	December	March
A. *Bank of Italy and Italian Exchange Office:*							
1) Official reserves:							
Gold	2,291.3	2,343.1	2,143.4	2,148.0	2,104.0	2,106.6	2,093.2
Convertible currencies	1,357.4	837.2	801.8	828.5	1,129.4	1,570.9	1,588.5
Total . . .	3,648.7	3,180.3	2,945,2	2,976.5	3,233.4	3,677.5	3,681.7
Net position with International Monetary Fund	207.7	225.7	0.7	0.7	125.0	141.4	173.9
Other reserves:							
U.S. Treasury Notes	200.0	200.0	150.0	—	—	—	—
Assets under General Arrangements to Borrow	—	—	—	—	—	5.0	5.0
Net position with European Monetary Fund	3.3	3.3	3.3	3.3	3.3	3.3	3.3
Short-term liabilities abroad	76.5	214.6	349.6	154.0	104.4	70.9	107.9
of which: central bank swaps	—	*50.0*	*150.0*	*94.4*	*57.3*	*29.9*	*12.2*
Net official reserves	3,983.2	3,394.7	2,749.6	2,826.5	3,257.3	3,756.3	3,756.0
2) Medium- and long-term assets:							
Medium-term U.S. Treasury Notes	13.1	13.1	10.2	1.8	—	—	—
Foreign currency bonds issued by the Italian government	366.4	350.5	345.2	347.0	336.8	335.1	335.7
Foreign currency bonds issued by non-residents	48.5	37.6	37.6	49.6	39.9	39.9	54.1
Lire bonds issued by non-residents	34.2	34.2	52.4	53.5	51.1	51.1	50.8
EPU balance	1.0	142.0	0.8	0.7	0.6	0.4	0.4
Consolidated credits and special accounts	147.9	16.7	143.4	140.3	131.7	123.0	125.1
Argentinian loan reserve account	17.5	1.6	16.7	15.9	15.9	15.1	15.1
Bilateral clearings	1.0	0.9	1.6	1.6	1.6	1.6	1.6
IBRD and European Investment Bank bonds held by Bank of Italy	4.2	4.1	4.2	4.4	4.6	4.5	4.5
Total 2) . . .	633.8	600.7	612.1	614.8	581.9	570.7	587.3
B. *Banks:*							
1) Convertible currencies	—1,051.2	— 965.4	— 837.3	— 703.0	— 585.3	— 633.8	— 584.8
2) Non-convertible currencies	0.1	1.7	2.3	2.5	2.5	2.9	3.3
3) Lire	— 317.1	— 290.7	— 222.0	— 209.7	— 222.9	— 181.2	— 178.8
Balance . . .	—1,368.2	—1,254.4	—1,057.0	— 910.2	— 805.7	— 812.1	— 760.3

the credit position of the Exchange Office rose by 317 million dollars, of which 294 are attributable to 1965. This is a reflection of the banks' higher lire liquidity and of rising interest rates on the Euro-currency market, which make it more profitable to draw on the Exchange Office's facilities rather than to borrow abroad.

In addition to their foreign exchange purchases from the Italian Exchange Office, banks also supplied themselves by forward operations, involving spot purchases of foreign currencies against lire with simultaneous forward sales. In the event, the banks' forward commitments (Table 25) increased by 58 million dollars during the second half of last year and by another 27 million in the first quarter of 1965.

TABLE 25

Foreign-Exchange Spot and Forward Position of Italian Banks

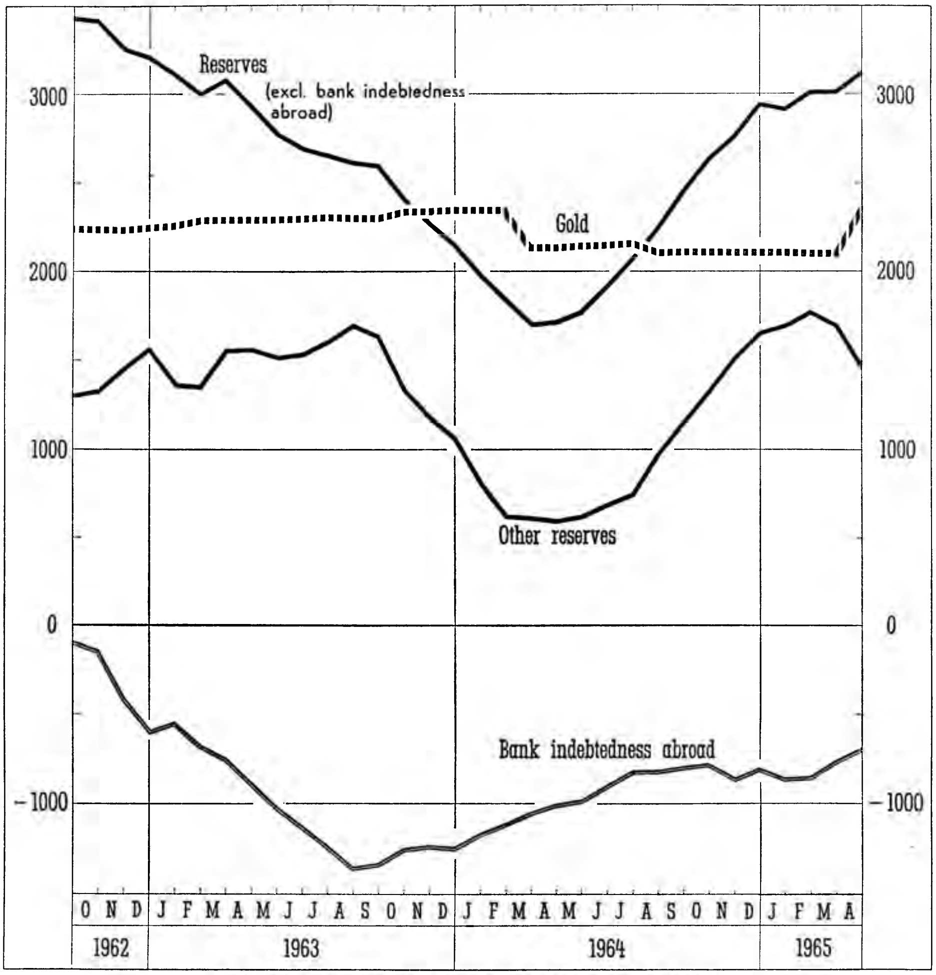
(End-month figures in million dollars)

Items	1963 Dec.	1964				1965 March
		March	June	Sept.	Dec.	
Position with Italian Exchange Office	305.4	313.5	314.2	306.2	329.2	622.7
of which:						
swaps with guaranteed rate	154.9	162.7	153.4	145.3	168.5	597.8
swaps without guaranteed rate	23.5	23.8	23.8	23.9	23.7	24.9
foreign exchange deposits	127.0	127.0	137.0	137.0	137.0	—
Working balances	19.1	11.1	12.6	8.3	6.2	8.4
Forward position (1)	— 18.1	5.0	8.3	41.2	66.6	93.3

(1) Balance of the banks' forward commitments at home and abroad. A positive balance means foreign exchange due to be paid, a negative balance means foreign exchange due to be received.

The Size and Composition of Official Reserves.— At the end of 1964, 2,107 out of the total 3,756 million dollars of Italy's official reserves were in gold (Chart 8). During the first quarter of the year reserves declined by 645 million dollars, since they were used to finance not only the current balance-of-payments deficit, but also repayments of bank debts abroad in the amount of 197 million dollars. During the following nine months, when the balance of payments brought in a surplus of 1,214 million dollars, the earlier depletion of convertible currency reserves was amply made good by an addition of 769 million dollars, but the gold reserve was further drawn down in the third quarter in connection with the increase in Italy's IMF quota, of which one quarter, or 57 million dollars, had to be paid in gold.

Chart 8



Official reserves and bank indebtedness abroad
(million dollars)

At the end of the year the International Monetary Fund, to meet the drawing by the United Kingdom, asked Italy for a lire loan in the equivalent of 5 million dollars, under the General Arrangements to Borrow decided upon in Paris in 1961.

As regards central bank facilities, Italy last June repaid her drawings on the credit line with the Federal Reserve System and the German Bundesbank, and at the same time arranged, and used, a reciprocal credit with the Swiss National Bank in the equivalent of 100 million dollars. Repayments on this latter credit line started immediately last June, and continued steadily until full settlement in April of this year. Italy took part in the central bank support action for sterling last October, by opening a credit line of 50 million dollars to the Bank of England; this was used and redeemed in the course of last year and a second credit line of 200 million dollars had been drawn on to half its amount by the end of April this year. The existing reciprocal credit between the Federal Reserve and the Bank of Italy was raised from 250 to 450 million dollars in April 1965, but at the same time the 100-million-dollar credit agreement with the United States Treasury was cancelled.

During the first quarter of this year net official reserves remained stationary, since an increase in liabilities mopped up the slight increment of gold and convertible currency reserves as well as an improvement of 33 million dollars in the credit position vis-à-vis the International Monetary Fund.

As regards the composition of the foreign exchange holdings of the Bank of Italy and the Italian Exchange Office, some 96 per cent of them were in U.S. dollars, mostly invested in U.S. Treasury Bonds. These and other minor investments last year yielded interest in the amount of 48 million dollars, which corresponds to an average return of 3.3 per cent. Over the course of the ten years ending in 1964 interest on official foreign exchange assets amounted to altogether 320 million dollars—more than 20 per cent of the convertible exchange holdings of the Bank of Italy and the Italian Exchange Office at the end of 1964.

From April 1964 onwards, renewed and consistent balance-of-payments surpluses lifted the country's reserves back to the peak figure of 1963, after they had lost 1,233 million dollars, including 148 million in gold, between August 1963 and March 1964 (Chart 8), under the combined impact of external deficits and repayments of bank debts abroad. In the twelve months from April 1964 to March 1965 reserves rose by 1,006 million dollars, including 787 million in convertible currencies; gold reserves, on the other hand, dropped by another 50 million dollars. The ratio of gold to net official reserves rose from 57.5 per cent in August 1963 to 78.0 per cent in March 1964, and then fell again to 55.7 per cent in March of this year. Deducting from net official reserves also the Italian banks' net indebtedness abroad, the corresponding ratios at the same dates would work out at 87.6, 126.6 and 69.9 per cent. In April of this year, gold assets previously credited to banks were transferred to the accounts of the Italian Exchange Office; this transaction, together with a gold purchase from the U.S. Treasury, raised the gold reserve by 261 million dollars back to its end-1963 level of 2,350 million dollars. Accordingly, the ratio of gold to net official reserves rose to 61.5 per cent, and its ratio to reserves net also of bank indebtedness to 75.4 per cent.

The Banking System's Foreign Transactions in Lire and Foreign Exchange.— Of the total reduction in the Italian banks' indebtedness abroad from 1,254 to 812 million dollars last year, 333 million are attributable to foreign exchange debts and 109 million to lire debts (Table 24). The contraction of exchange debts was to some extent reflected in the position of Italian banks on the Eurodollar market (Table 26), where their net liabilities fell by 107 million to 684 million dollars.

The banks' overall position abroad and their foreign exchange position at home, as summarized in Table 27, will be seen to have changed from net liabilities of 2 million dollars at the end of 1963 to net assets of 231 million at the end of 1964. Lire liabilities dropped by 221 million dollars, and foreign exchange assets rose by 12 million.

TABLE 26

Eurodollar Assets and Liabilities of Italian Banks (1)

(End-month figures in million dollars)

Country	1963		1964				1965
	September	December	March	June	September	December	March
United Kingdom:							
Assets	120.0	143.4	83.6	60.0	101.2	203.2	239.9
Liabilities	492.2	437.2	345.2	321.4	331.8	423.3	257.1
Balance	– 372.2	– 293.8	– 261.6	– 261.4	– 230.6	– 220.1	– 17.2
Switzerland:							
Assets	120.2	133.4	150.0	157.8	152.4	152.9	115.8
Liabilities	140.0	147.6	143.7	149.2	170.1	197.6	206.8
Balance	– 19.8	– 14.2	6.3	8.6	– 17.7	– 44.7	– 91.0
France:							
Assets	53.5	44.9	24.2	33.2	36.7	51.7	86.5
Liabilities	207.4	197.9	144.5	152.3	123.1	166.2	134.3
Balance	– 153.9	– 153.0	– 120.3	– 119.1	– 86.4	– 114.5	– 47.8
Belgium:							
Assets	18.1	12.2	6.6	5.3	5.0	2.4	9.9
Liabilities	60.5	43.4	39.9	33.0	30.9	50.5	50.3
Balance	– 42.4	– 31.2	– 33.3	– 27.7	– 25.9	– 48.1	– 40.4
Germany:							
Assets	16.3	13.0	3.8	2.5	7.3	6.2	4.5
Liabilities	82.7	24.1	49.8	12.4	5.5	6.0	3.6
Balance	– 66.4	– 11.1	– 46.0	– 9.9	1.8	0.2	0.9
Netherlands:							
Assets	5.6	3.0	5.5	8.8	2.5	5.8	4.9
Liabilities	46.3	40.4	35.7	17.5	28.6	50.9	50.4
Balance	– 40.7	– 37.4	– 30.2	– 8.7	– 26.1	– 45.1	– 45.5
Mediterranean countries:							
Assets	16.7	4.1	9.3	9.8	8.3	13.7	15.4
Liabilities	107.8	139.6	150.1	117.3	96.5	120.5	91.6
Balance	– 91.1	– 135.5	– 140.8	– 107.5	– 88.2	– 106.8	– 76.2
Latin American countries:							
Assets	48.0	47.2	47.9	48.0	45.2	45.9	15.2
Liabilities	43.8	42.9	47.5	46.3	53.5	51.4	61.8
Balance	4.2	4.3	0.4	1.7	– 8.3	– 5.5	– 46.6
Other countries:							
Assets	84.5	72.4	46.8	47.5	42.2	51.0	69.4
Liabilities	277.9	191.7	165.2	166.3	136.4	150.6	135.3
Balance	– 193.4	– 119.3	– 118.4	– 118.8	– 94.2	– 99.6	– 65.9
Total:							
Assets	482.9	473.6	377.7	372.9	400.8	532.8	561.5
Liabilities	1,458.6	1,264.8	1,121.6	1,015.7	976.4	1,217.0	991.2
Balance	– 975.7	– 791.2	– 743.9	– 642.8	– 575.6	– 684.2	– 429.7

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(1) Assets include balances with foreign correspondents in sight and time deposits as well as short-term investments; liabilities include foreign accounts of banks, financial institutions, companies and personal clients abroad.

TABLE 27

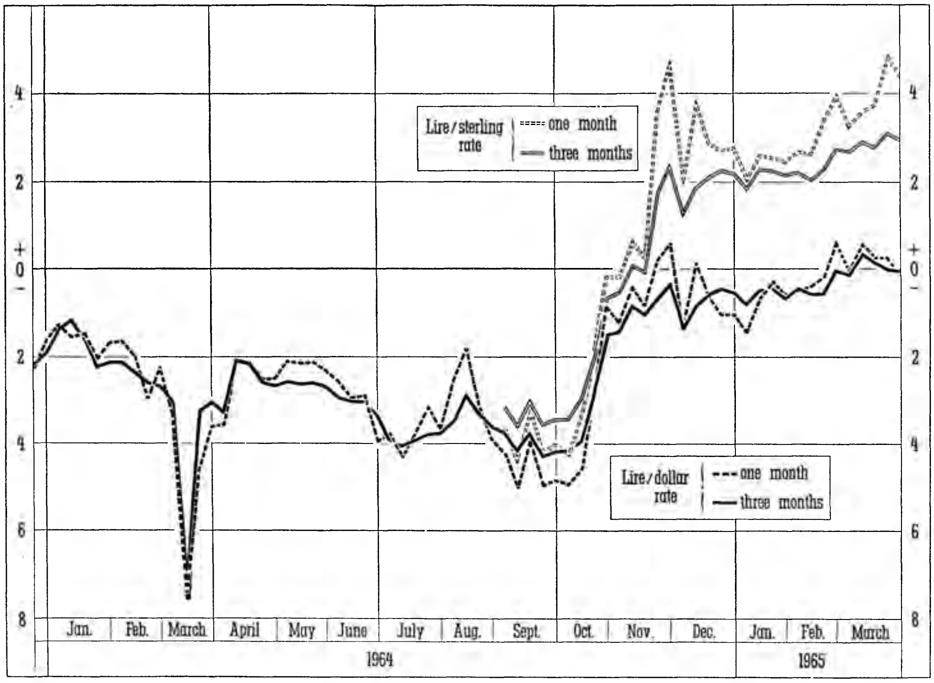
The Italian Banks' Overall Position Abroad and Foreign Exchange Position at Home

(End-month figures in million dollars)

Items	1963 December	1964				1965 March
		March	June	August	December	
ASSETS						
A. *Assets abroad:*						
1. In convertible currencies	1,177.8	1,122.0	1,102.8	1,098.2	1,306.5	1,249.7
2. In non-convertible currencies	3.7	4.5	4.7	5.2	5.1	5.6
3. In lire	89.6	100.5	119.2	99.8	124.3	116.7
4. Forward commitments abroad	1,768.7	1,734.3	1,674.7	1,236.4	969.1	1,293.6
a) *foreign exchange receivable*	*1,768.7*	*1,734.3*	*1,607.4*	*1,168.9*	*895.6*	*1,211.1*
b) *lire receivable*	—	—	*67.3*	*67.5*	*73.5*	*82.5*
Total A	3,039.8	2,961.3	2,901.4	2,439.6	2,405.0	2,665.6
B. *Domestic assets in foreign exchange:*						
1. Credits to	1,725.1	1,621.7	1,487.3	1,394.6	1,511.4	1,698.4
a) *clients*	*1,661.3*	*1,581.8*	*1,451.6*	*1,340.6*	*1,462.8*	*1,636.0*
b) *others*	*63.8*	*39.9*	*35.7*	*54.0*	*48.6*	*62.4*
2. Forward commitments in Italy	0.9	0.9	106.5	75.8	25.6	2.8
Total B	1,726.0	1,622.6	1,593.8	1,470.4	1,537.0	1,701.2
C. *Total assets* (A + B)	4,765.8	4,583.9	4,495.2	3,910.0	3,942.0	4,366.8
LIABILITIES						
D. *Liabilities abroad:*						
1. In convertible currencies	2,155.8	1,973.3	1,817.4	1,671.2	1,943.0	1,845.4
2. In non-convertible currencies	2.1	2.2	2.3	2.8	2.2	2.3
3. In lire	380.3	322.4	328.8	322.7	305.5	295.5
4. Forward commitments abroad	1,756.0	1,720.4	1,663.1	1,248.6	966.4	1,282.7
a) *foreign exchange payable*	*1,718.2*	*1,696.6*	*1,663.1*	*1,248.6*	*966.4*	*1,282.7*
b) *lire payable*	*37.8*	*23.8*	—	—	—	—
Total D	4,294.2	4,018.3	3,811.6	3,245.3	3,217.1	3,425.9
E. *Domestic liabilities in foreign exchange:*						
1. Deposits from	440.7	440.8	437.6	465.9	472.9	378.3
a) *clients*	*233.1*	*259.4*	*261.0*	*271.5*	*287.6*	*288.0*
b) *others*	*207.6*	*181.4*	*176.6*	*194.4*	*185.3*	*90.3*
2. Forward commitments in Italy	33.3	43.6	59.1	37.3	21.4	24.5
Total E	474.0	484.4	496.7	503.2	494.3	402.8
F. *Total liabilities* (D + E)	4,768.2	4,502.7	4,308.3	3,748.5	3,711.4	3,828.7
BALANCES						
G. *Net position vis-à-vis abroad:*						
On spot transactions	—1,267.1	—1,070.9	— 921.8	— 793.5	— 814.8	— 771.2
On forward transactions	12.7	13.9	11.6	— 12.2	2.7	10.9
foreign exchange	*50.5*	*37.7*	— *55.7*	— *79.7*	— *70.8*	— *71.6*
lire	— *37.8*	— *23.8*	*67.3*	*67.5*	*73.5*	*82.5*
Balance (A — D)	—1,254.4	—1,057.0	— 910.2	— 805.7	— 812.1	— 760.3
H. *Net foreign exchange position in Italy:*						
On spot transactions	1,284.4	1,180.9	1,049.7	928.7	1,038.5	1,320.1
On forward transactions	— 32.4	— 42.7	47.4	38.5	4.2	— 21.7
foreign exchange	— *32.4*	— *42.7*	*47.4*	*38.5*	*4.2*	— *21.7*
Balance (B — E)	1,252.0	1,138.2	1,097.1	967.2	1,042.7	1,298.4
I. *Overall position* (H + G)	— 2.4	81.2	186.9	161.5	230.6	538.1
On spot transactions	17.3	110.0	127.9	135.2	223.7	548.9
On forward transactions	— 19.7	— 28.8	59.0	26.3	6.9	— 10.8
foreign exchange	*18.1*	— *5.0*	— *8.3*	— *41.2*	— *66.6*	— *93.3*
lire	— *37.8*	— *23.8*	*67.3*	*67.5*	*73.5*	*82.5*

The Forward Rate of the Lira.— The forward quotations of the lira last year (Chart 9) reflected the changing expectations of foreign and Italian financial circles in line with the vicissitudes and later improvements in the balance of payments and the domestic economic situation; nor did they escape the impact of speculative movements in connection with events abroad.

CHART 9



Lire/dollar and lire/sterling forward rates

Premium (+) or discount (—) of the lira forward rate against the spot rate (per cent per year)

It will be recalled from last year's Annual Report how speculative forward dealings in lire assumed crisis proportions in March 1964 and lifted the lira's discount against the dollar to 7.50 per cent, inducing business men and banks to rush for cover. The Washington agreements of last March brought the forward discount down to 3–3.50 per cent by the end of the month, and the improvement went on for two more months. In June pressure on the lira increased again and with it the covering operations of importers and of Italian and foreign banks. The Bank of Italy had to spend 132 million dollars on supporting the currency, which was 46 million more than the cost of interventions in March which were falling due in June.

The summer brought some respite, but in September renewed weakness of the forward rate again lifted the discount above 4 per cent. However, this time the strain had nothing to do with apprehensions about the future of the lira, but was simply the backwash of earlier interventions. The three-month commitments entered into in March and extended for another three months in June became due in September, and in a narrow market the currency suffered heavily even in the absence of large-scale speculation.

From the last quarter of the year onwards the forward rate of the lira against the dollar has been improving steadily, well into the early months of this year. At the same time the lira was at a premium, and indeed occasionally considerably so, against sterling, after the rise of Bank Rate to 7 per cent in the United Kingdom.

These developments, together with the Italian banks' own foreign exchange position, were reflected in the volume and composition of foreign exchange credits extended by Italian banks to domestic clients. There was a sharp contrast between the period January-August, when these credits contracted steadily by a cumulative total of 323 million dollars, and the remainder of the year, when they expanded again by 124 million dollars. At the end of December, 1,463 million dollars were outstanding in such credits, and another 173 million were extended during the first three months of 1965.

U.S. dollars accounted for a steadily increasing share of the total, having begun the year with 47.5 per cent and ending it with 66 per cent. Credits in Swiss francs decreased correspondingly, but in January 1965, when comparative interest rates made Swiss francs cheaper, there was a large-scale shift to the latter at the expense of U.S. dollars—so much so that by the end of March dollars represented 50 per cent and Swiss francs 44.5 per cent of the total.

VI. *The Budget and the Finances of the Public Sector*

Conflicting tendencies were apparent last year in the various compartments which are customarily considered as belonging to the public sector.

The government's budget policy was governed by the intention to keep expenditure within limits compatible with the twin objective of letting the rest of the economy meet its foreseeable expansion needs and contributing to financial stability.

It has not been easy, in recent months, to try to balance the budget, because the economy kept needing more and more support. It is true that additional public expenditure of this kind is productive expenditure, but it often has a high capital/output ratio, especially in the short run. The initial estimates for the 1965 administrative budget and its actual application during the first few months of this year clearly reflect the afore-mentioned twin objective. In their turn, the Treasury's cash requirements last year remained close to the, admittedly rather high, 1963 figures, even though claims on the Central Post Office Savings Fund increased appreciably. To some extent this result was achieved by accumulating new arrears, which means in effect that expenditures committed for last year were postponed to the more or less indefinite future. To judge by early figures this year, the Treasury's cash position is likely to be rather worse in 1965 (even allowing for the fact that the figures are not strictly comparable with those of previous years, because of the change-over last January to a fiscal year coinciding with the calendar year).

Both local authorities and autonomous government agencies saw their expenditures last year get more and more out of line with their revenue. As regards at least local authorities, the government did make an attempt to exercise stricter control over their budgeting and expenditure, but while this was no doubt a step in the right direction, it failed to redress the situation in anything like a decisive manner; for this reason government is now inclined to adopt a more radical approach involving far-reaching reforms, as indeed is evident in the national five-year plan. These are the sectors where imbalances most threaten to get out of hand and where financial reorganization cannot be postponed any longer.

In welcome contrast, the whole set of Social Insurance Funds last year again recorded conspicuous surpluses, some of which were used for security purchases on the capital market. However, there is little likelihood that this situation will continue, given that I.N.P.S., the National Social Security Agency, has to face new heavy expenditure under provisions already adopted or about to pass into law.

To go back to the government's own administrative budget, the figures for 1964 and 1965 show a return to the tendency for total revenue (excluding public debt operations) to cover a higher portion of expenditure (Table 28). They also show encouraging progress in public saving, as evidenced by the growing excess of investment over the deficit.

Table 28

Government Finance

(administrative budget; billion lire)

Fiscal years (*a*)	Net revenue (*b*)	Net expenditure (*b*)	Ratio of revenue to expenditure (per cent)	Net deficit			Public investment	Surplus of investment over deficit
				Current section	Capital movements	Total		
1	2	3	4=2 : 3	5	6	7=5+6=2—3	8	9=7+8
1961/62	4,621	5,005	*92.3*	— 299	— 85	— 384	1,071	687
1962/63	5,296	5,843	*90.6*	— 442	— 105	— 547	1,223	676
1963/64	6,007	6,505	*92.3*	— 412	— 86	— 498	1,169	671
1964 - 2nd half	3,138	3,570	*87.9*	— 288	— 144	— 432	705	273
1964/65	6,153	6,575	*93.6*	— 359	— 63	— 422	1,160	738
1965	6,628	7,092	*93.5*	— 295	— 169	— 464	1,294	830

(*a*) The figures for 1961/62, 1962/63, 1963/64 and the second half of 1964 are provisional outturn, those for 1964/65 and 1965 are initial estimates.

(*b*) Current items plus capital items other than public debt operations.

No major change can be seen as between the 1963 and 1964 figures regarding the Treasury's cash requirements for its own purposes and those of the Central Post Office Savings Fund, as well as certain expenditures by autonomous government agencies. In both years these requirements were not far short of 900 billion lire (Table 29).

TABLE 29

Treasury Cash Requirements and their Coverage

(billion lire)

Items	1963		1964		1965 1st quarter
	1st quarter	Total	1st quarter	Total	
Overall cash requirements					
Budget deficit (—)	— 265	— 336	— 77	2	— 552
Treasury operations (*a*)	122	57	80	— 106	274
Extrabudgetary operations	— 64	— 586	— 164	— 773	— 109
Total . . .	— 207	— 865	— 161	— 877	— 387
Coverage of overall cash requirements					
Long-term borrowing, excl. Bank of Italy (*b*)	— 171	— 210	73	45	47
Postal savings	119	422	70	321	84
Treasury Bills, excl. Bank of Italy	50	— 131	77	72	191
Short-term borrowing, excl. Bank of Italy	8	17	— 4	13	— 20
Borrowing from Bank of Italy, excl. current account	— 108	— 59	— 26	374	— 162
Bank of Italy advances on current account (*c*)	309	826	— 29	52	247
Total . . .	207	865	161	877	387
(Commercial banks' holdings of stockpiling bills)	— *7*	— *76*	— *15*	— *5*	—

(*a*) Receipts (+) and payments (—).
(*b*) Including foreign debts.
(*c*) Increase (+) or decrease (—) in the Treasury's debt.

As regard their coverage, however, there was a profound difference in public debt policy during the two years. For the first time in a long while the new bonds issued last year by the Credit Consortium for Public Works on behalf of the Treasury were placed directly with the public, instead of being taken up by other government agencies. Accordingly, the long-term debt last year helped to finance the deficit, even if the amount involved was not large; in 1963, by contrast, extinction of maturing bonds did much to raise the Treasury's claims on the money market. The reasons underlying these divergent policies have, in substance, to do with liquidity control and also with the changed conditions of the capital market. As regards short-term debts, Treasury Bills increased again last year after a conspicuous diminution in 1963.

For all these reasons the Treasury had to borrow far less from the Bank of Italy last year; the total amount involved fell from 767 to 426 billion lire. In particular, the Treasury's debit balance on current account increased by only 52 billion, as against 826 billion in 1963, because the Bank made the bulk of its funds available in the form of government security purchases (Treasury Bills and others, in the amount of about 330 billion lire).

VII. *The Capital and Money Markets and the Control of Liquidity*

The Stock Market.— Net of redemptions and duplications, the proceeds of security issues last year were 1,927 billion lire, a striking 442 billion more than in 1963 and even 136 billion more than in 1962.

In a situation of falling investment, a large increase in the claims of firms on the market for finance capital is a sure sign of contracting self-financing margins.

The net flow of funds channelled into investment through the stock market amounted to 6.3 per cent of gross domestic product and to 29.5 per cent of gross fixed investment (5.3 and 22.4 per cent, respectively, in 1963). Both ratios are distinctly higher than elsewhere in the European Economic Community.

Apart from the sheer size of security issues last year, another noteworthy feature was their strong concentration in the second half of the year. Equity issues were fairly evenly distributed, but three fifths of all bond issues (800 out of a total of 1,372 billion lire) were floated in the latter half of 1964. These large sums could be raised only thanks to massive bond purchases on the part of the banking system, where the liquidity position had eased greatly by that time. The very volume of bank purchases brought down yield rates, which indeed diminished steadily from July onwards.

New Net Security Issues

(billion

Subscribers	Government stock and bonds issued for Treasury account									
	Govt. stock	Bonds for Treasury account					Total	Special credit institutes		
		Railways	Green Plan	Rural Housing	Road Agency	Total		Industr.	Others	Total
										1 9
Bank of Italy and Italian Exchange Office	2.5	— 0.2	16.8	—	—	16.6	19.1	3.0	0.3	3.3
Banks	8,9	— 1.0	54.8	—	—	53.8	62.7	92.7	46.0	138.7
Banking associations	— 1.3	— 2.2	4.3	—	—	2.1	0.8	— 14.3	17.2	2.9
Central Post Office Savings Fund	— 1.0	3.1	—	—	—	3.1	2.1	15.4	—	15.4
Social Insurance Funds	0.1	1.9	1.0	—	—	2.9	3.0	15.6	13.4	29.0
Insurance companies	3.5	5.7	2.1	—	—	7.8	11.3	0.5	21.2	21.7
Private investors and companies	— 20.6	20.9	36.0	—	—	56.9	36.3	171.0	132.0	303.0
Total	**— 7.9**	**28.2**	**115.0**	—	—	**143.2**	**135.3**	**283.9**	**230.1**	**514.0**
										1 9
Bank of Italy and Italian Exchange Office	— 47.4	11.7	65.3	—	—	77.0	29.6	2.3	— 0.1	2.2
Banks	29.1	— 7.2	0.5	—	—	— 6.7	22.4	190.5	129.8	320.3
Banking associations	— 0.4	— 0.3	— 2.1	—	—	— 2.4	— 2.8	59.6	— 12.4	47.2
Central Post Office Savings Fund	— 43.2	48.1	51.0	—	—	99.1	55.9	31.2	24.8	56.0
Social Insurance Funds	1.1	— 0.4	1.9	—	—	1.5	2.6	48.5	22.7	71.2
Insurance companies	1.3	— 0.8	— 0.9	—	—	— 1.7	— 0.4	29.2	6.3	35.5
Private investors and companies	— 49.0	— 10.4	— 5.1	19.2	—	3.7	— 45.3	76.1	109.7	185.8
Total	**— 108.5**	**40.7**	**110.6**	**19.2**	—	**170.5**	**62.0**	**437.4**	**280.8**	**718.2**
										1 9
Bank of Italy and Italian Exchange Office	— 23.1	— 1.4	8.3	—	—	6.9	— 16.2	— 0.3	— 0.1	— 0.4
Banks	— 31.3	— 5.5	— 3.1	—	—	— 8.6	— 39.9	214.7	102.5	317.2
Banking associations	0.6	—	3.0	—	—	3.0	3.6	— 2.4	— 7.3	— 9.7
Central Post Office Savings Fund	— 10.0	46.3	97.6	—	—	143.9	133.9	30.0	23.1	53.1
Social Insurance Funds	— 4.4	— 0.3	— 0.3	—	—	— 0.6	— 5.0	37.5	21.3	58.8
Insurance companies	— 3.7	— 0.2	—	—	—	— 0.2	— 3.9	6.4	12.4	18.8
Private investors and companies	— 128.5	— 9.9	— 4.8	— 0.6	—	— 15.3	— 143.8	183.9	153.0	336.9
Total	**— 200.4**	**29.0**	**100.7**	**— 0.8**	—	**129.1**	**— 71.3**	**469.8**	**304.9**	**774.7**
										1 9
Bank of Italy and Italian Exchange Office	61.4	— 0.6	101.9	10.3	—	111.6	173.0	10.3	—	10.3
Banks	2.5	— 4.0	1.9	—	—	— 2.1	0.4	51.9	67.9	119.8
Banking associations	— 3.9	0.5	— 0.1	—	—	0.4	— 3.5	43.1	20.5	63.6
Central Post Office Savings Fund	— 18.8	— 5.9	— 67.4	—	37.2	— 36.1	— 54.9	105.8	45.9	151.7
Social Insurance Funds	— 0.2	— 0.5	—	—	—	— 0.5	— 0.7	118.2	54.9	173.1
Insurance companies	— 1.3	0.7	0.7	—	—	1.4	0.1	7.3	5.5	12.8
Private investors and companies	— 47.5	— 7.4	91.9	— 0.6	—	83.9	36.4	137.9	45.2	183.1
Total	**— 7.8**	**— 17.2**	**128.9**	**9.7**	**37.2**	**158.6**	**150.8**	**474.5**	**239.9**	**714.4**

by Types and Subscribers

lire)

TABLE 30

Bonds									
Government-controlled agencies and companies				Business companies	International institutions	Total	Shares	Total	Subscribers
ENEL	ENI	IRI	Total						
6 1									
—	—	— 0.1	— 0.1	—	2.1	5.3	—	24.4	Bank of Italy and Italian Exchange Office
—	18.1	10.0	28.1	— 6.7	9.5	169.6	—	232.3	Banks
—	— 6.9	—	— 6.9	— 1.2	—	— 5.2	—	— 4.4	Banking associations
—	—	— 0.7	— 0.7	—	—	14.7	—	16.8	Central Post Office Savings Fund
—	— 0.4	— 0.4	— 0.8	1.2	—	29.4	—	32.4	Social Insurance Funds
—	4.7	4.7	9.4	0.5	—	31.6	—	42.9	Insurance companies
—	30.4	56.0	86.4	143.6	3.4	536.4	514.6	1,087.3	Private investors and companies
—	**45.9**	**69.5**	**115.4**	**137.4**	**15.0**	**781.8**	**514.6**	**1,431.7**	Total
6 2									
—	—	4.7	4.7	0.2	17.4	24.5	—	54.1	Bank of Italy and Italian Exchange Office
—	19.4	6.9	26.3	36.6	7.1	390.3	—	412.7	Banks
—	35.3	13.4	48.7	0.2	—	96.1	—	93.3	Banking associations
—	—	— 1.1	— 1.1	—	—	54.9	—	110.8	Central Post Office Savings Fund
—	— 1.0	— 0.9	— 1.9	5.5	—	74.8	—	77.4	Social Insurance Funds
—	— 2.7	— 2.8	— 5.5	1.6	—	31.6	—	31.2	Insurance companies
—	13.8	— 25.0	— 11.2	161.3	5.5	341.4	715.5	1,011.6	Private investors and companies
—	**64.8**	**— 4.8**	**60.0**	**205.4**	**30.0**	**1,013.6**	**715.5**	**1,791.1**	Total
6 3									
—	—	— 0.2	— 0.2	5.7	0.1	5.2	—	— 11.0	Bank of Italy and Italian Exchange Office
—	41.2	13.2	54.4	3.8	3.3	378.7	—	338.8	Banks
—	— 12.8	8.0	— 4.8	13.6	0.2	— 0.7	—	2.9	Banking associations
147.9	—	— 2.3	145.6	—	—	198.7	—	332.6	Central Post Office Savings Fund
—	—	— 1.1	— 1.1	10.5	—	68.2	—	63.2	Social Insurance Funds
—	—	1.2	1.2	— 2.1	—	17.9	—	14.0	Insurance companies
—	44.0	36.2	80.2	62.4	11.0	490.5	397.5	744.2	Private investors and companies
147.9	**72.4**	**55.0**	**275.3**	**93.9**	**14.6**	**1,158.5**	**397.5**	**1,484.7**	Total
6 4									
—	—	— 0.5	— 0.5	— 0.9	— 1.0	7.9	—	180.9	Bank of Italy and Italian Exchange Office
100.8	52.5	24.4	177.7	9.8	— 0.8	306.5	—	306.9	Banks
65.8	30.4	0.8	97.0	— 5.9	—	154.7	—	151.2	Banking associations
110.1	—	— 1.1	109.0	—	—	260.7	—	205.8	Central Post Office Savings Fund
9.6	38.8	—	48.4	8.9	—	230.4	—	229.7	Social Insurance Funds
—	0.6	0.6	1.2	0.7	—	14.7	—	14.8	Insurance companies
2.1	— 12.0	51.5	41.6	19.9	1.8	246.4	554.8	837.6	Private investors and companies
288.4	**110.3**	**75.7**	**474.4**	**32.5**	—	**1,221.3**	**554.8**	**1,926.9**	Total

Total bond issues increased from 1,087 to 1,372 billion lire last year, under the impact, largely, of higher claims by the public sector. The Treasury, E.N.E.L. (the National Electricity Board), E.N.I. (the large government-controlled petroleum company) and I.R.I. (the holding and management agency for government-controlled industry) between them raised 625 billion lire on bonds last year, or 46 per cent of the total (204 billion, or 19 per cent, in 1963). These funds were needed for current government programmes, to carry on investment projects already put in hand by government-controlled companies, and to pay the instalments due on compensation for nationalized electricity companies.

Equity issues, at 555 billion lire, were 157 billion up on 1963, but still fell considerably short of the 1962 peak of 715 billion. About one third of the proceeds came from abroad, and went largely into one single Italian company.

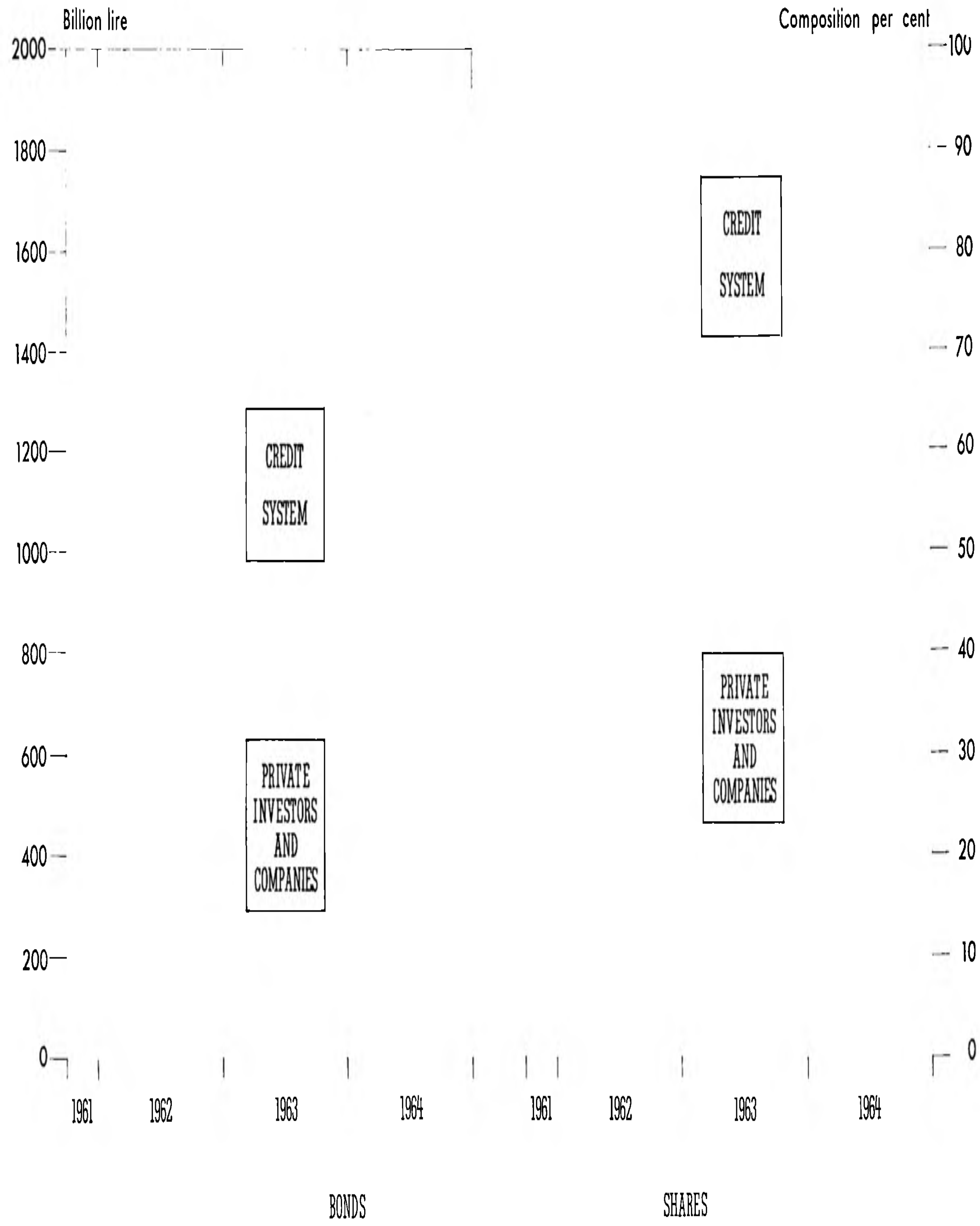
Share issues accounted for 29 per cent of total new security issues last year. While this is a slightly better proportion than in 1963, it remains well below the 38 per cent of the years 1961 and 1962 (Chart 10).

The banking system, the Central Post Office Savings Fund and Social Insurance Funds between them took up more than half of total (share and bond) issues last year and so contributed decisively to the widening of the new issue market. But this also meant that a lot of investment capital again came from money market sources, as has been happening ever since 1961. Before then, something like four fifths of annual security issues were taken up by private investors and companies; last year they absorbed only 44 per cent, or 852 billion lire, and in 1963 51 per cent, or 758 billion lire (including in both years a small amount taken up by insurance companies).

More particularly, private investors' and companies' bond subscriptions fell from one third (361 billion) of the total in 1963 to hardly more than one fifth (298 billion) last year. Social Insurance Funds raised their share from 6 to 17 per cent by taking in a total of 230 billion lire's worth of bonds, against 63 billion in 1963. An unchanged 62 per cent proportion of bond

BOND AND SHARE ISSUES BY CATEGORIES OF SUBSCRIBERS

(twelve-month changes at quarterly intervals)



issues placed with banks and with the Central Post Office Savings Fund meant an increase, in absolute terms, from 663 to 845 billion lire (Table 30).

Private investors and companies thus proved even more reluctant than before to put their savings into fixed-interest securities, so that the credit system had to come to the rescue. During the first half of the year, when major public issues had to be accommodated, the main subscribers were the Bank of Italy and the Central Post Office Savings Fund; later, when bank liquidity improved, commercial banks came to the fore.

During the last two months both the Electricity Board and government-controlled industry needed to raise large funds, and in order not to deprive other issuers of the resources which reach the stock market, the monetary authorities decided to release for this purpose part of the compulsory reserves of savings banks.

As a result of large-scale subscriptions to the 1964 issues by the banks, the ratio between their (and their banking associations') holdings of medium- and long-term bonds and bank deposits rose to 17 per cent (15.6 per cent at the end of 1963) (Table 31).

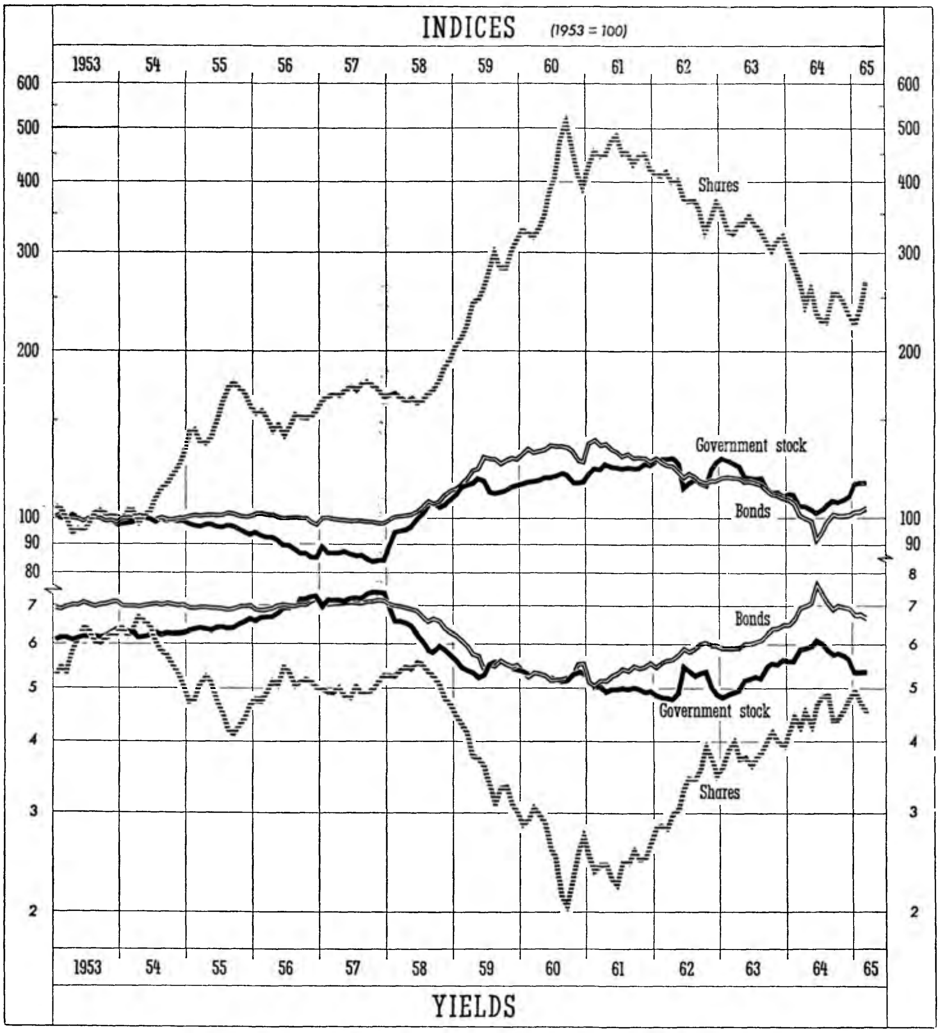
The unwillingness of private investors and companies to subscribe to bonds last year was reflected in a fall of the proportion of total fixed-interest securities outstanding in the hands of this category of investors: at the end of 1963 they owned 56.5 per cent of the total, at the end of last year only 51.4 per cent. Taking all bonds and shares together, private investors and companies held more than three quarters of the total outstanding in December 1964.

As regards stock exchange quotations, bond prices recovered in the second half of last year when fears for the future purchasing power of the lira began to recede and bank liquidity eased. Fiscal concessions with respect to transfer charges also helped to some extent.

The prices of government stock at first continued the slide they had begun in December 1962, and touched bottom in June

1964 at 1958 levels; subsequently, they made good the year's loss and by December were back at the levels of December 1963 (Chart 11).

Chart 11

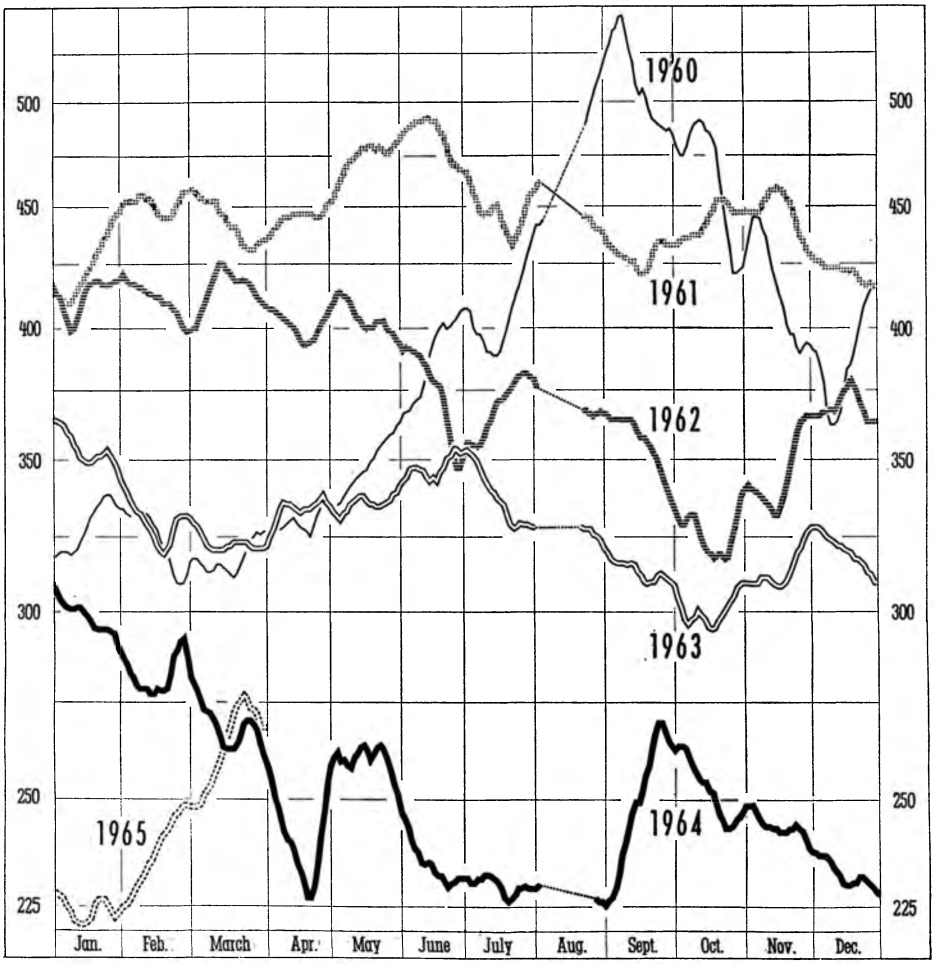


Indices of stock exchange prices and security yields

(1953 = 100; logarithmic scale)

Other bond prices followed the same pattern, only more so. At the close of the year the price index had fallen by 6.9 per cent from 108.7 to 101.2 over twelve months, and consequently yields had risen by half a point, from 6.42 to 6.90 per cent.

CHART 12



Daily index of share prices at the Milan stock exchange
(moving five-days averages; logarithmic scale; 1953 = 100)

TABLE 31

Fixed-interest Security Holdings (1) and Deposits of Banks and Banking Associations

(end-month figures at book values, in billion lire)

Date	Banks			Savings banks and banking associations			Total		
	Securities	Deposits	Ratio per cent	Securities	Deposits	Ratio per cent	Securities	Deposits	Ratio per cent
Dec. 1961	664.3	8,976.1	*7.4*	994.9	2,949.6	*33.7*	1,659.2	11,925.7	*13.9*
1962	928.8	10,677.3	*8.7*	1,236.4	3,504.2	*35.3*	2,165.2	14,181.5	*15.3*
1963	1,130.9	11,970.9	*9.4*	1,376.0	4,057.8	*33.9*	2,506.9	16,028.7	*15.6*
1964	1,224.5	12,960.7	*9.4*	1,740.5	4,490.1	*38.8*	2,965.0	17,450.8	*17.0*

(1) Excluding Treasury Bills.

Shares, finally, had their fourth year of almost uninterrupted decline. Prices fell heavily during the first half of the year and the recovery in April and May proved short-lived; the subsequent six months of ups and downs left share prices at the end of the year down at the June trough (Chart 12). Early this year there was some improvement, thanks to a good dividend season and a few hopeful signs of recovery in industrial production; this helped shares to make good the losses they suffered during the last quarter of 1964.

Special Credit Institutes.— Heavy demand for credit last year involved the special credit institutes in great efforts to raise new loanable resources. The capital market proved difficult during the first six months of the year, when investable funds were scarce and the cost of loan capital was correspondingly high; in these conditions the credit institutes raised more money abroad and borrowed more from the banks at short term. Later, the institutes were very active placing their bonds at home, but while fund-raising costs slightly declined at that time, this was not enough to prevent the cost of long-term funds from rising above their 1963 level.

All told, the special credit institutes last year added another 1,207 billion lire to the total of their loans outstanding, or just a little more than in 1963 (Table 32). The importance of this kind of credit in financing investment can be measured by

Table 32

The Special Credit Institutes' Operations and Loans Outstanding

Type of loan	Billion lire outstanding 31 Dec. 1964	Annual increase in			
		1963		1964	
		billion lire	per cent	billion lire	per cent
Medium- and long-term loans	6,798.1	984.0	*20.3*	965.5	*16.6*
of which: tied export credits . . .	193.9	44.9	*39.8*	39.6	*25.7*
Short-term credits to agriculture . .	573.0	20.4	*4.0*	42.9	*8.1*
Loans for Treasury account	901.7	138.7	*24.4*	193.8	*27.4*
Total . . .	8,272.8	1,143.1	*19.3*	1,202.2	*17.0*
Loans to developing countries	49.7	26.0	*135.4*	4.5	*10.0*
Grand total . . .	8,322.5	1,169.1	*19.7*	1,206.7	*17.0*

TABLE 33

Special Credit Institutes' Loans and Bonds Outstanding (1)

Period	Industrial credit institutes (2)				Land & Building credit institutes		Agricultural credit inst.		Total	
	Loans			Bonds	Loans	Bonds	Land improvement cred.	Bonds	Loans	Bonds
	Ordinary	On special funds	Total							
	End-period figures in billion lire									
1962 December	3,078.7	174.6	3,253.3	2,057.9	1,284.3	1,209.1	311.0	69.7	4,848.6	3,336.7
1963 March	3,229.0	166.5	3,395.5	2,206.3	1,387.3	1,305.5	320.7	74.0	5,103.5	3,585.8
June	3,400.4	158.0	3,558.4	2,341.9	1,455.9	1,379.1	328.6	74.2	5,342.9	3,795.2
September	3,538.2	152.6	3,690.8	2,437.4	1,555.3	1,459.4	339.3	80.0	5,585.4	3,976.8
December	3,721.4	145.2	3,866.6	2,581.1	1,619.4	1,533.2	346.6	81.1	5,832.6	4,195.4
1964 March	3,878.1	147.1	4,025.2	2,663.6	1,697.4	1,589.4	357.7	85.4	6,080.3	4,338.4
June	3,991.2	140.5	4,131.7	2,733.7	1,742.7	1,652.0	364.7	86.0	6,239.1	4,471.7
September	4,184.5	148.3	4,332.8	2,878.6	1,843.6	1,744.5	372.9	87.1	6,549.3	4,710.2
December	4,353.6	165.8	4,519.4	3,070.9	1,899.2	1,804.9	379.5	86.7	6,798.1	4,962.5
	Increase in billion lire									
1963 First quarter	150.3	— 8.1	142.2	148.4	103.0	96.4	9.7	4.3	254.9	249.1
Second quarter	171.4	— 8.5	162.9	135.6	68.6	73.6	7.9	0.2	239.4	209.4
Third quarter	137.8	— 5.4	132.4	95.5	99.4	80.3	10.7	5.8	242.5	181.6
Fourth quarter	183.2	— 7.4	175.8	143.7	64.1	73.8	7.3	1.1	247.2	218.6
Total	642.7	— 29.4	613.3	523.2	335.1	324.1	35.6	11.4	984.0	858.7
1964 First quarter	156.7	1.9	158.6	82.5	78.0	56.2	11.1	4.3	247.7	143.0
Second quarter	113.1	— 6.6	106.5	70.1	45.3	62.6	7.0	0.6	158.8	133.3
Third quarter	193.3	7.8	201.1	144.9	100.9	92.5	8.2	1.1	310.2	238.5
Fourth quarter	169.1	17.5	186.6	192.3	55.6	60.4	6.6	— 0.4	248.8	252.3
Total	632.2	20.6	652.8	489.8	279.8	271.7	32.9	5.6	965.5	767.1
	Percentage increase over preceding December									
1963 First quarter	*4.9*	*— 4.6*	*4.4*	*7.2*	*8.0*	*8.0*	*3.1*	*6.2*	*5.3*	*7.5*
Second quarter	*10.4*	*— 9.5*	*9.4*	*13.8*	*13.4*	*14.1*	*5.7*	*6.5*	*10.2*	*13.7*
Third quarter	*14.9*	*— 12.6*	*13.4*	*18.4*	*21.1*	*20.7*	*9.1*	*14.8*	*15.2*	*19.2*
Fourth quarter	*20.9*	*— 16.8*	*18.9*	*25.4*	*26.1*	*26.8*	*11.4*	*16.4*	*20.3*	*25.7*
1964 First quarter	*4.2*	*1.3*	*4.1*	*3.2*	*4.8*	*3.7*	*3.2*	*5.3*	*4.2*	*3.4*
Second quarter	*7.2*	*— 3.2*	*6.9*	*5.9*	*7.6*	*7.7*	*5.2*	*6.0*	*7.0*	*6.6*
Third quarter	*12.4*	*2.1*	*12.1*	*11.5*	*13.8*	*13.8*	*7.6*	*7.4*	*12.3*	*12.3*
Fourth quarter	*17.0*	*14.2*	*16.9*	*19.0*	*17.3*	*17.7*	*9.5*	*6.9*	*16.6*	*18.3*

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(1) Excluding loans to the Treasury and corresponding bonds, short-term credits to agriculture and stockpiling finance.

(2) A new series, based on different statistical material, starts as of the end of 1963; figures for earlier periods were reconstructed on the same basis to make them comparable.

Bank

(Changes in

Causes of change	1962 1st quarter	1962 2nd quarter	1962 3rd quarter	1962 4th quarter	1962 Year
1. AUTONOMOUS FACTORS					
a) Foreign sector	— 57.8	— 1.3	204.3	— 106.3	38.9
b) Treasury	93.8	— 187.3	235.5	330.0	472.0
c) Other sectors	40.9	— 14.6	26.7	— 54.1	— 1.1
d) less Liquid assets in the hands of the public	— 135.3	107.7	232.5	477.2	682.1
e) less Compulsory bank reserves and deposits	189.4	37.0	91.7	176.0	494.1
Total 1.	22.8	— 347.9	142.3	— 483.6	— 666.4
2. INTERVENTION BY MONETARY AUTHORITIES					
a) Medium- and long-term public debt operations	— 4.5	8.9	15.9	1.2	21.5
b) Open market operations	15.0	— 4.2	29.9	32.9	73.6
c) Changes in rulings on compulsory bank reserves	200.0	—	—	—	200.0
d) Rediscounts and deferred clearing house payments	— 12.3	— 1.2	8.2	22.5	17,2
e) Open credit line with Bank of Italy	1.7	8.1	42.3	120.9	173.0
of which: *advances drawn*	*13.8*	*29.2*	— *22.5*	*132.2*	*152.7*
disposable margin	— *12.1*	— *21.1*	*64.8*	— *11.3*	*20.3*
f) Foreign exchange operations with banks	— 102.2	89.9	— 14.0	5.6	— 20.7
Total *a)* through *f)*	97.7	101.5	82.3	183.1	464.6
g) Short-term foreign credits to banks	— 18.7	44.9	13.8	254.0	294.0
Total 2.	79.0	146.4	96.1	437.1	758.6
3. BANK LIQUIDITY (1 + 2)	101.8	— 201.5	238.4	— 46.5	92.2

Table 34

Liquidity

billion lire)

1963					1964					1965
1st quarter	2nd quarter	3rd quarter	4th quarter	Year	1st quarter	2nd quarter	3rd quarter	4th quarter	Year	1st quarter
— 166.3	— 260.2	— 63.9	— 290.2	— 780.6	— 272.9	136.3	314.7	305.8	483.9	41.5
205.7	— 128.2	166.6	372.5	616.6	126.8	— 44.8	150.0	384.1	616.1	385.5
— 4.9	— 16.0	48.2	— 60.3	— 33.0	40.1	— 88.3	60.5	— 16.9	— 4.6	— 2.0
13.1	165.0	118.2	455.4	751.7	— 151.0	24.2	120.5	577.5	571.2	— 247.2
280.4	97.4	12.0	21.1	410.9	90.1	67.3	— 43.4	188.5	302.5	90.6
— 259.0	— 666.8	20.7	— 454.5	—1,359.6	— 45.1	— 88.3	448.1	— 93.0	221.7	581.6
171.0	9.3	10.1	8.9	199.3	— 73.1	17.9	6.2	— 7.4	— 56.4	— 46.9
0.1	18.0	28.9	141.5	188.5	19.0	185.9	51.0	20.6	276.5	1.2
51.1	15.2	13.6	46.3	126.2	12.9	— 2.9	— 3.7	128.0	134.3	43.1
— 6.0	83.9	— 13.9	255.1	319.1	62.8	24.5	— 231.9	— 47.3	— 191.9	— 119.7
14.8	42.0	15.7	71.7	144.2	— 45.1	31.8	60.3	13.8	60.8	12.5
— *53.5*	*159.6*	— *76.6*	*48.1*	*77.6*	*69.0*	— *19.7*	— *113.0*	*11.7*	— *52.0*	— *76.3*
68.3	— *117.6*	*92.3*	*23.6*	*66.6*	— *114.1*	*51.5*	*173.3*	*2.1*	*112.8*	*88.8*
— 0.8	— 8.1	— 3.2	1.9	— 10.2	— 2.2	11.9	— 5.5	5.7	9.9	— 164.8
230.2	160.3	51.2	525.4	967.1	— 25.7	269.1	— 123.6	113.4	233.2	— 274.6
72.1	223.4	104.1	— 59.1	340.5	— 121.8	— 81.2	— 50.4	12.5	— 240.9	— 40.5
302.3	383.7	155.3	466.3	1,307.6	— 147.5	187.9	— 174.0	125.9	— 7.7	— 315.1
43.3	— 283.1	176.0	11.8	— 52.0	— 192.6	99.6	274.1	32.9	214.0	266.5

the ratio of the institutes' new medium- and long-term loans, including those for account of the Treasury, to total gross fixed investment. This ratio was 17.8 per cent last year, 16.9 per cent in 1963 and 20.3 per cent in 1962. Looking a little further into the past, a ratio of 14.0 per cent for the three-year period 1959-1961 compares with 18.3 per cent for 1962-1964, when firms had to rely more heavily on outside funds to finance their investment and when the Treasury needed more money for government programmes. Important as these figures show the special credit institutes to be as a source of investment finance, they are likely to play an even bigger part this year, especially through operations for account of the Treasury.

Medium- and long-term loans, by which the institutes finance directly productive investment, increased last year at a slightly lower rate than of late, but still by 966 billion lire (984 billion in 1963). The slow-down was due mostly to building credits and, to a lesser extent, to agricultural improvement loans; industry and public works received more (Table 33).

Bank Liquidity.— Major changes took place last year in the relative weight and in the direction of both the autonomous and the policy factors which go to determine bank liquidity (Table 34).

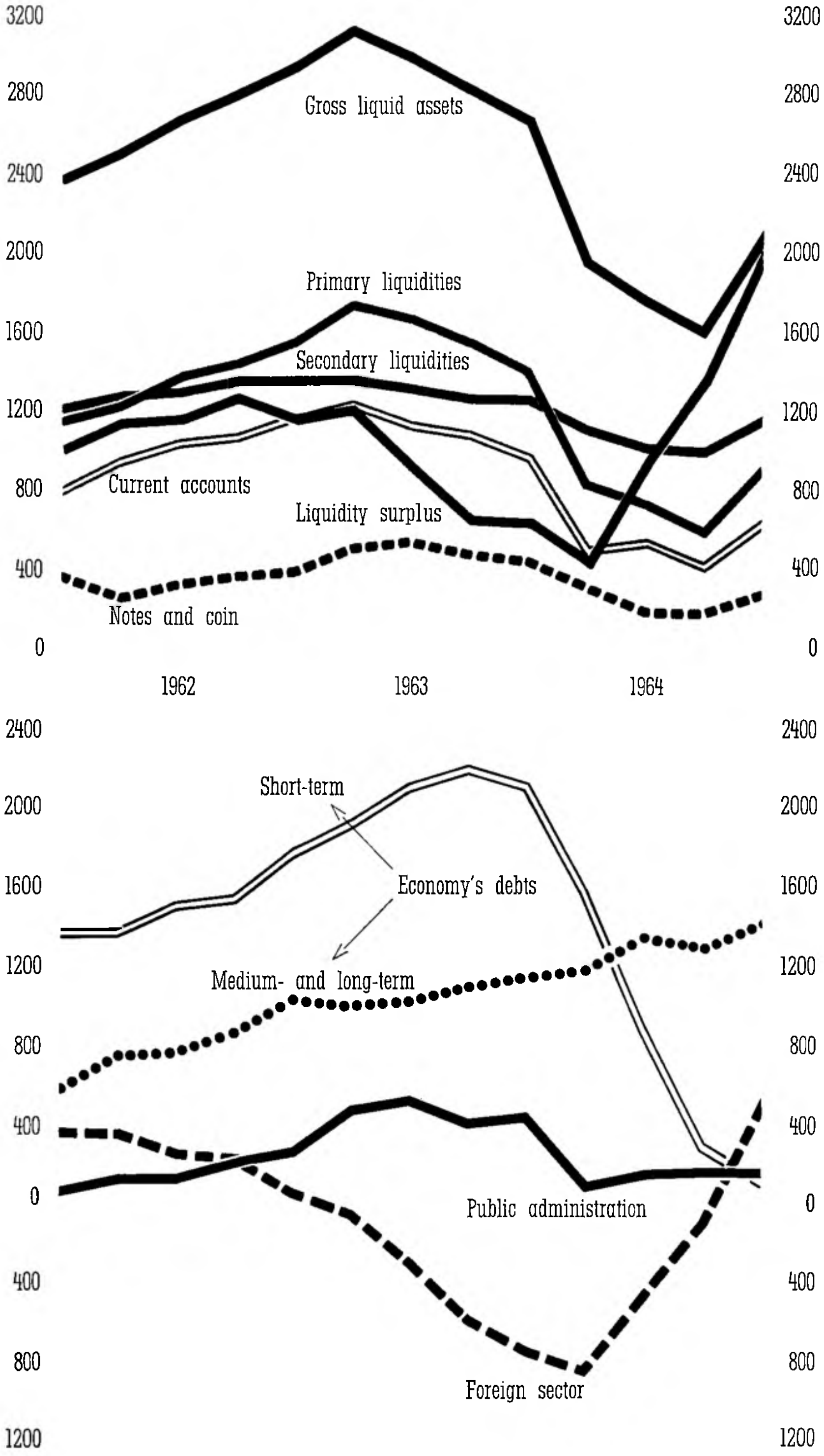
Two features stand out among the effects of autonomous factors: (a) the balance of payments did much to expand liquidity last year, whereas in 1963 it had mopped up large amounts; (b) liquid assets held by the public increased much less fast and had a correspondingly lesser restrictive effect on bank liquidity.

The liquidity gains due to autonomous factors and to open market operations (changes in the forms of investment of compulsory reserves had almost identical effects in 1963 and 1964) enabled the banks to repay large parts of the debts they had previously contracted with the Bank of Italy and abroad. Both these two factors, therefore, reversed their direction: they had strongly expanded bank liquidity in 1963, and reduced it appreciably in 1964.

These changes make the policy line quite clear. In 1963, the monetary authorities counteracted the liquidity-restricting effects

THE ECONOMY'S LIQUIDITY AND ITS COUNTERPARTS

(12-month changes at monthly intervals, in billion lire)



of the external deficit; last year they left the liquidities generated by the external surplus in the system and on the whole added further to them. This did not mean that all separate policy measures uniformly worked in the same direction; for reasons of particular purposes of control the authorities sometimes restricted bank liquidity in one way, only to expand it strongly in another. For instance, steps were taken to lighten the burden of the Italian banks' indebtedness abroad, even though this meant absorbing liquidity; on the other hand, the weakness of the capital market led the authorities to give their open market operations a frankly liquidity-creating aspect, and the same is true of the composition of compulsory bank reserves. The amount of recourse to the central bank, which also figures under intervention by the monetary authorities, depended less on the latter than on the banks themselves and ultimately on the slack demand for bank credits.

The events of 1963 had already shown how difficult it is for monetary policy alone to safeguard both internal and external balance in the presence of rising costs; the surfeit of liquidity last year confirmed that easy money policy is not enough to sustain the rate of production.

The Economy's Liquidity. — The gross liquid assets of the Economy (defined as all the country's economic sectors except the Treasury—that is, Government and the Central Post Office Saving Fund—and except financial enterprises) consist of its holdings of short-term credit instruments, and their counterparts are the Economy's own debts plus those of the Treasury and the foreign sector. Deduction of the Economy's short-term debts gives its net liquid assets, or so-called liquidity surplus. The absolute figures involved are shown in Table 35 and twelve-month changes over the last three years in Chart 13.

If gross liquid assets are divided into primary liquidities (banknotes and coin, current accounts) and secondary liquidities (savings deposits, short-term securities), the former are seen to have fluctuated much more widely, both in the upswing and the downswing phases. This is largely due to the cyclical sensitivity of current accounts. But the note circulation also displayed con-

The Economy's Liquidity

(changes in

Items	1962				
	1st quarter	2nd quarter	3rd quarter	4th quarter	Year
LIQUID ASSETS					
Primary liquidities					
Notes and coin	— 217.7	114.3	153.4	339.9	389.9
Current bank accounts, cheques and drafts	114.9	250.0	246.3	489.8	1,101.0
Current Post Office accounts	21.3	— 0.7	14.3	33.3	68.2
Total . . .	— 81.5	363.6	414.0	863.0	1,559.1
Secondary liquidities					
Savings deposits at banks	213.2	149.3	272.7	499.0	1,134.2
Post Office savings book and savings certificates	63.4	29.8	56.5	153.0	302.7
Other deposits	— 7.3	— 18.8	— 2.3	— 39.0	— 67.4
Short-term securities	5.0	— 7.7	2.5	— 16.4	— 16.6
Total . . .	274.3	152.6	329.4	596.6	1,352.9
TOTAL . . .	192.8	516.2	743.4	1,459.6	2,912.0
COUNTERPART: NET FINANCE TO					
Foreign sector from					
Bank of Italy and Italian Exchange Office	— 85.0	8.9	176.1	207.9	307.9
Banks	27.2	— 10.2	28.2	— 314.2	— 269.0
Total . . .	— 57.8	— 1.3	204.3	— 106.3	38.9
Treasury					
Short-term credits from					
Bank of Italy and Ital. Exchange Office	— 59.1	— 182.2	102.5	327.3	188.5
Banks	77.8	11.4	96.2	— 112.6	72.8
Economy	83.4	— 4.9	81.6	139.7	299.8
Total . . .	102.1	— 175.7	280.3	354.4	561.1
Government bonds	8.0	3.7	— 7.0	14.9	19.6
Total . . .	110.1	— 172.0	273.3	369.3	580.7
less investments and credits by the Central Post Office Savings Fund	61.1	89.2	78.0	113.4	341.7
Total . . .	49.0	— 261.2	195.3	255.9	239.0
Economy					
Short-term credits from					
Bank of Italy and Ital. Exchange Office	— 0.5	1.3	0.9	— 1.1	0.6
Banks	121.1	420.8	273.5	930.6	1,746.0
Total . . .	120.6	422.1	274.4	929.5	1,746.6
Medium- and long-term credits from					
Banks	16.6	31.9	38.2	78.3	165.0
Central Post Office Savings Fund	48.3	87.7	60.8	90.2	287.0
Total . . .	64.9	119.6	99.0	168.5	452.0
Bonds subscribed by					
Bank of Italy and Ital. Exchange Office	2.1	— 7.2	0.8	9.2	4.9
Banks	88.0	105.2	123.6	169.6	486.4
Central Post Office Savings Fund	12.8	1.5	17.2	23.2	54.7
Total . . .	102.9	99.5	141.6	202.0	546.0
Shares and equity participations	40.0	— 9.3	— 7.0	16.7	40.4
Total . . .	328.4	631.9	508.0	1,316.7	2,785.0
Other items	— 126.8	146.8	— 164.2	— 6.7	— 150.9
Total . . .	201.6	778.7	343.8	1,310.0	2.634.1
TOTAL . . .	192.8	516.2	743.4	1,459.6	2,912.0

and its Counterpart

TABLE 35

billion lire)

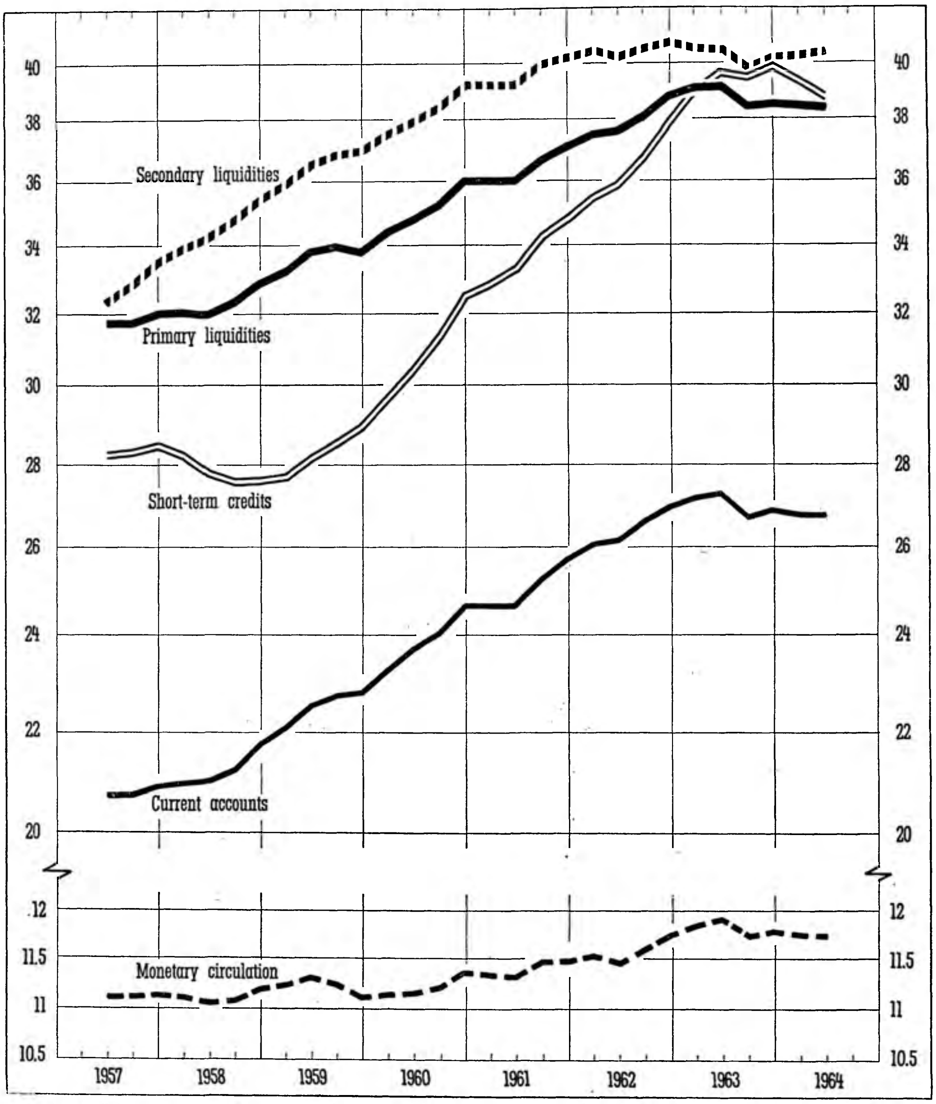
1 9 6 3					1 9 6 4					1965 1st quarter
1st quarter	2nd quarter	3rd quarter	4th quarter	Year	1st quarter	2nd quarter	3rd quarter	4th quarter	Year	
— 98.1	153.5	74.1	311.4	440.9	— 220.2	24.4	62.4	404.0	270.6	— 332,1
156.8	100.6	243.7	376.0	877.1	— 262.3	172.8	115.9	578.2	604.6	63.8
46.0	34.0	— 24.4	26.5	82.1	7.9	— 3.0	— 21.6	36.6	19.9	5.1
104.7	288.1	293.4	713.9	1,400.1	— 474.6	194.2	156.7	1,018.8	895.1	— 263.2
211.3	118.9	208.0	474.3	1,012.5	61.0	10.7	168.5	597.4	837.6	190.6
72.9	37.9	56.9	172.0	339.7	62.2	24.3	38.4	175.7	300.6	79.1
13.2	11.5	28.1	— 26.8	26.0	13.3	— 12.1	46.6	— 22.0	25.8	— 7.3
— 17.6	— 55.6	— 17.5	— 27.0	— 117.7	2.2	— 8.4	1.2	— 6.6	— 11.6	8.0
279.8	112.7	275.5	592.5	1,260.5	138.7	14.5	254.7	744.5	1,152.4	270.4
384.5	400.8	568.9	1,306.4	2,660.6	— 335.9	208.7	411.4	1,763.3	2,047.5	7.2
— 70.2	— 21.0	62.9	— 346.2	— 374.5	— 396.3	44.6	249.4	309.8	207.5	9.1
— 96.1	— 239.2	— 126.8	56.0	— 406.1	123.4	91.7	65.3	— 4.0	276.4	32.4
— 166.3	— 260.2	63.9	— 290.2	— 780.6	— 272.9	136.3	314.7	305.8	483.9	41.5
202.0	— 74.0	128.1	511.1	767.2	— 55.0	129.4	47.3	304.0	425.7	84.8
56.9	— 40.4	31.3	— 135.5	— 87.7	56.7	27.3	93.7	— 88.9	88.8	168.9
112.4	13.5	46.2	147.3	319.4	71.0	2.3	61.1	177.2	311.6	86.5
371.3	— 100.9	205.6	522.9	998.9	72.7	159.0	202.1	392.3	826.1	340.2
— 48.2	1.7	0.9	9.3	— 36.3	3.1	— 9.9	5.2	— 1.4	— 3.0	19.7
323.1	— 99.2	206.5	532.2	962.6	75.8	149.1	207.3	390.9	823.1	359.9
56.1	107.7	127.1	250.8	541.7	148.9	303.9	120.3	135.3	708.4	88.6
267.0	— 206.9	79.4	281.4	420.9	— 73.1	— 154.8	87.0	255.6	114.7	271.3
— 2.0	—	— 0.1	0.4	— 1.7	— 0.5	0.3	—	— 0.1	— 0.3	1.7
275.9	594.0	388.9	786.1	2,044.9	— 241.2	— 103.1	— 189.0	642.5	109.2	— 419.0
273.9	594.0	388.8	786.5	2.043.2	— 241.7	— 102.8	— 189.0	642.4	108.9	— 417.3
55.6	46.5	74.7	78.0	254.8	56.7	54.7	74.5	83.6	269.5	43.4
53.3	89.7	98.2	110.0	351.2	129.9	127.9	75.4	118.8	452.0	91.7
108.9	136.2	172.9	188.0	606.0	186.6	182.6	149.9	202.4	721.5	135.1
5.5	— 0.5	0.6	— 0.6	5.0	. .	— 1.1	5.7	5.4	10.0	0.1
118.1	69.3	105.9	84.7	378.0	23.0	36.1	65.8	336.2	461.1	104.2
2.8	18.0	28.9	140.8	190.5	19.0	176.0	44.9	16.5	256.4	— 3.1
126.4	86.8	135.4	224.9	573.5	42.0	211.0	116.4	358.1	727.5	101.2
— 57.2	20.9	—	5.8	— 30.5	— 14.3	3.4	0.4	— 0.9	— 11.4	8.0
452.0	837.9	697.1	1,205.2	3,192.2	— 27.4	294.2	77.7	1,202.0	1,546.5	— 173.0
— 168.2	30.0	— 143.7	110.0	— 171.9	37.5	— 67.0	— 68.0	— 0.1	— 97.6	— 132.6
283.8	867.9	553.4	1,315.2	3,020.3	10.1	227.2	9.7	1,201.9	1,448.9	— 305.6
384.5	400.8	568.9	1,306.4	2,660.6	— 335.9	208.7	411.4	1,763.3	2,047.5	7.2

siderable cyclical fluctuations, which seem to be attributable to two main reasons, namely, the great changes in the rate of increase in gross domestic product at current prices over the three years, and the shift in income distribution to the benefit of labour incomes during the cycle and more especially in 1963. Changes in the propensity to consume may have been a subsidiary factor. The monetary circulation increased sharply especially in the second half of 1962 and the first half of 1963; this was a reflection of the wage inflation, the income effects of which were yet accentuated by a relative increase in consumer spending on imported goods. The ratio of monetary circulation to national income rose very rapidly during that year (Chart 14).

If all the short-term funds reaching financial enterprises (here and subsequently always understood to include insurance companies) were employed in short-term uses, the Economy's liquidity surplus would exactly match the combined liquidity shortfall of the foreign sector and the Treasury. But in actual fact a growing portion of the flow of short-term funds from the Economy was returned to it in the form of medium- and long-term credits, which are not imputed against its gross liquid assets. It follows that the Economy's net liquid assets are increased by the amount of its short-term deposits which come back to it in long-term credits. In other words, the credit system creates liquidity in two ways: (a) it creates gross liquidity to the extent that a given degree of bank liquidity, deriving from the liquidity shortfall of the foreign sector and the Treasury and the system's own operations with the central bank, enables it to grant credits, which either generate deposits or expand the monetary circulation; and (b) it creates net liquidity to the extent that it uses deposits to back long-term credits.

As can be seen from Chart 13, gross liquidity (and all its components, that is, monetary circulation, current accounts, savings deposits) has a long-run tendency to grow faster than gross domestic product, and similarly liquid assets with an inherently slower turnover rate tend to increase faster than the quicker ones. Thus (up to 1961) primary liquidity grew more than secondary liquidity, and within the former, current accounts more than note circulation.

CHART 14



Percentage ratio of liquidities and short-term credits to gross national product

Moving annual averages (centred on the middle of the span) of quarterly figures for liquidities and credits over annual GNP; logarithmic scale

Now, the means with the quickest turnover rate are those which change hands through a payment, or a chain of payments, in every production period. They include banknotes paid by firms as wages to their workers and spent by the latter to buy services and consumer goods, and they include also current account balances transferred by firms to their suppliers. The volume of these payments tends to keep in step with the income flow, and the monetary means involved vary in direct proportion with these payments (reflecting also other influences such as changes in the pay period, or in the structure of expenditure).

Similarly, the volume of short-term credit demand for working capital tends to vary in proportion with the income flow, apart from changes in the length of the production period.

In this first-approximation model, a given volume of liquid asset formation generates, on the assumption of constant velocity, a corresponding expansion of national income in money terms and a proportional demand for short-term credit. Looking at the relationship between credits and deposits from the other direction, it can also be said that short-term credit demand sufficient to initiate new production cycles in plant requiring no further finance imparts to any given volume of liquid means of payment the precise velocity of circulation required to raise income proportionally.

However, the rise in the liquidity/income and short-term-credit/income ratios in Italy during the last few years does not fit into this model. What happened was that low-velocity funds accumulated in the banks under the impact of domestic cyclical factors (such as an unwillingness to invest in the stock market, active competition for deposits among the banks) and institutional factors which, in Italy as abroad, tend to draw bank deposits more and more into longer and higher-yielding uses. Because these funds originated (especially in the most recent cyclical phases) in saving and disinvestment rather than in a simultaneous expansion of short-term credit associated with income production, they were until the middle of 1963 matched among the banks' assets by credits which, while formally short-term, were in fact only partly so; more recently, they backed also large credits of a formally long-term nature. If the banks had not been allowed to use part of these deposits in *de facto* and now even *de iure* medium and long credits, two results would have followed: (1) short rates would have been lower, and long rates higher, than they actually were, and this different pattern of interest rates would not necessarily have been conducive to higher income growth; (2) even more liquidity would have accumulated in the banks in excess of credits.

In short, it can be said that the banks' expansion of their medium- and long-term lending owed as much to the sheer mechanics of the economy as to monetary policy.

But monetary policy is ultimately responsible for this part of liquidity also, in so far as there is a problem of how, and to what extent, these low-velocity funds are to be channelled back to the capital market by cutting back the financing function of the banking system—which is all the more necessary as these funds are often available on call, for instance in current accounts, and could thus become dangerous in a cyclical upswing.

The mere fact that the liquidity/income ratio of 80 per cent in Italy is higher than in almost any other developed country lends force to the argument that this ratio should not be allowed to rise any higher.

Because domestic liquidity can finance import demand, its level is relevant also for the country's foreign exchange reserves, which constitute its external liquidity.

With the return to a balance-of-payments surplus, the ratio between net foreign reserves and total liquid assets has begun to rise again, though moderately, after having fallen to its lowest point in ten years in 1963 (5.8 per cent). Now this ratio is 7.3 per cent, and 14.9 per cent if only primary liquidities are counted.

The Economy's Total Financial Assets.— Through the medium of liquidity control, monetary policy influences not only the money supply, but also the volume of transactions in other assets, as well as the willingness to hold them. In this way, monetary policy governs the size of both the money and the capital market.

Changes in the Economy's total financial assets and their counterpart during the last four years are shown in Table 36.

TABLE 36

The Economy's Total Financial Assets and their Counterpart

(billion lire)

Items	Changes in				Amount on 31-12-1964
	1961	1962	1963	1964	
FINANCIAL ASSETS					
Liquidid assets					
primary liquidities	1,159.4	1,559.1	1,400.1	895.1	12,372.2
secondary liquidities	1,205.4	1,352.9	1,260.5	1,152.4	12,797.5
Total	2,364.8	2,912.0	2,660.6	2,047.5	25,169.7
Securities					
government bonds	55.7	— 48.0	— 169.6	51.8	1,439.0
other bonds	581.3	437.3	565.3	487.4	4,090.5
shares	483.3	696.3	444.2	570.9	10,780.4
Total	1,120.3	1,085.6	839.9	1,110.1	16,309.9
Other financial assets	209.1	466.7	382.8	408.7	3,909.9
TOTAL	3,694.2	4,464.3	3,883.3	3,566.3	45,389.5
COUNTERPART					
Short-term credits to					
Foreign sector	362.7	38.9	— 780.6	483.9	2,218.5
Treasury:					
Government	— 34.6	190.0	574.8	504.4	4,449.4
Central Post Office Savings Fund	274.6	371.1	424.1	321.7	3,618.7
Total	240.0	561.1	998.9	826.1	8,068.1
Economy	1,356.7	1,776.8	2,097.8	124.4	11,679.7
Total	1,959.4	2,376.8	2,316.1	1,434.4	21,966.3
Medium- and long-term credits to					
Treasury	125.3	— 21.5	— 199.3	56.4	2,212.5
less credits by:					
Government	100.4	97.7	120.7	60.5	1,451.5
Central Post Office Savings Fund	267.3	341.7	541.7	708.4	3,223.5
Total	— 242.4	— 460.9	— 861.7	— 712.5	—2,462.5
Economy	1,977.2	2,548.4	2,428.9	2,844.4	25,885.7
Total	1,734.8	2.087.5	1,567.2	2,131.9	23,423.2
TOTAL	3,694.2	4,464.3	3,883.3	3,566.3	45,389.5
SUMMARY BY SECTORS					
Foreign sector	362.7	38.9	— 780.6	483.9	2,218.5
Treasury (net)	— 2.4	100.2	137.2	113.6	5,605.6
Economy	3,333.9	4,325.2	4,526.7	2,968.8	37,565.4
TOTAL	3,694.2	4,464.3	3,883.3	3,566.3	45,389.5

In synthesis, this table can be reduced to the following few figures, which retain the distinction between the short and the long term:

	Foreign Sector	Treasury	Economy	Foreign Sector	Treasury	Economy
		1961			1962	
Short	− 362	− 240	+1,008	− 39	− 561	+1,135
Long	—	+ 242	− 648	—	+ 461	− 996
Total . . .	− 362	− 2	+ 360	− 39	− 100	+ 139
		1963			1964	
Short	+ 781	− 999	+ 563	− 484	− 826	+1,924
Long	—	+ 862	−1,207	—	+ 712	−1,326
Total . . .	+ 781	− 137	− 644	− 484	− 114	+ 598

The Economy's liquidity surplus served, last year, to finance the deficit of the other two sectors, while in 1963 it had been the foreign sector which financed the others.

The Treasury's liquidity surplus on long-term operations means that this sector gave back to the Economy more than it had received from the latter through the same kind of operations; to do this, the Treasury had to draw to some extent on short-term assets it had received from the Economy.

In other words, the Economy last year to all intents and purposes financed its own net long-term requirements through the intermediary of money-creating bodies, to which it advanced a greatly increased volume of net short-term credit.

Some idea of the magnitude of short-term means used to cover the Economy's long-term requirements can be gained from a comparison between the Economy's long-term shortfall and its overall requirements, as calculated from Table 36. In 1961 this shortfall amounted to 33 per cent of total requirements, it then rose to 39 per cent in 1962 and 50 per cent in 1963, and last year fell back slightly to 47 per cent. This confirms in the broader setting of total financial assets what was already said in commenting upon Table 35, namely, that more and more of the money supply is being drawn into financing long-term requirements.

The figures in the last column of Table 36 yield useful comparisons between the various categories of assets, which convey some idea of the comparative part played by the capital market. One significant indicator is the ratio between securities owned by the Economy and primary liquidities: at the end of 1964, the former amounted to 130 per cent of the latter.

Monetary Circulation.— Last year's cyclical developments were clearly reflected also in the note circulation, which rose from 3,698.6 billion lire in December 1963 to 3,914.1 billion at the end of last year. This increase of 215.5 billion was less than half the preceding year's 464.2 billion. More meaningful, perhaps, than these aggregate figures, is the gradual reduction of the absolute volume of increase over the course of the year, as represented graphically in Chart 15.

For the purposes of this Chart, moving monthly averages were calculated from the daily figures of monetary circulation, and centred on the middle of the span, considering as many terms as there are working days in each corresponding month. Instead of entering the average value for every working day of the year, the median value of each week was taken as representative, for the convenience of graphical representation.

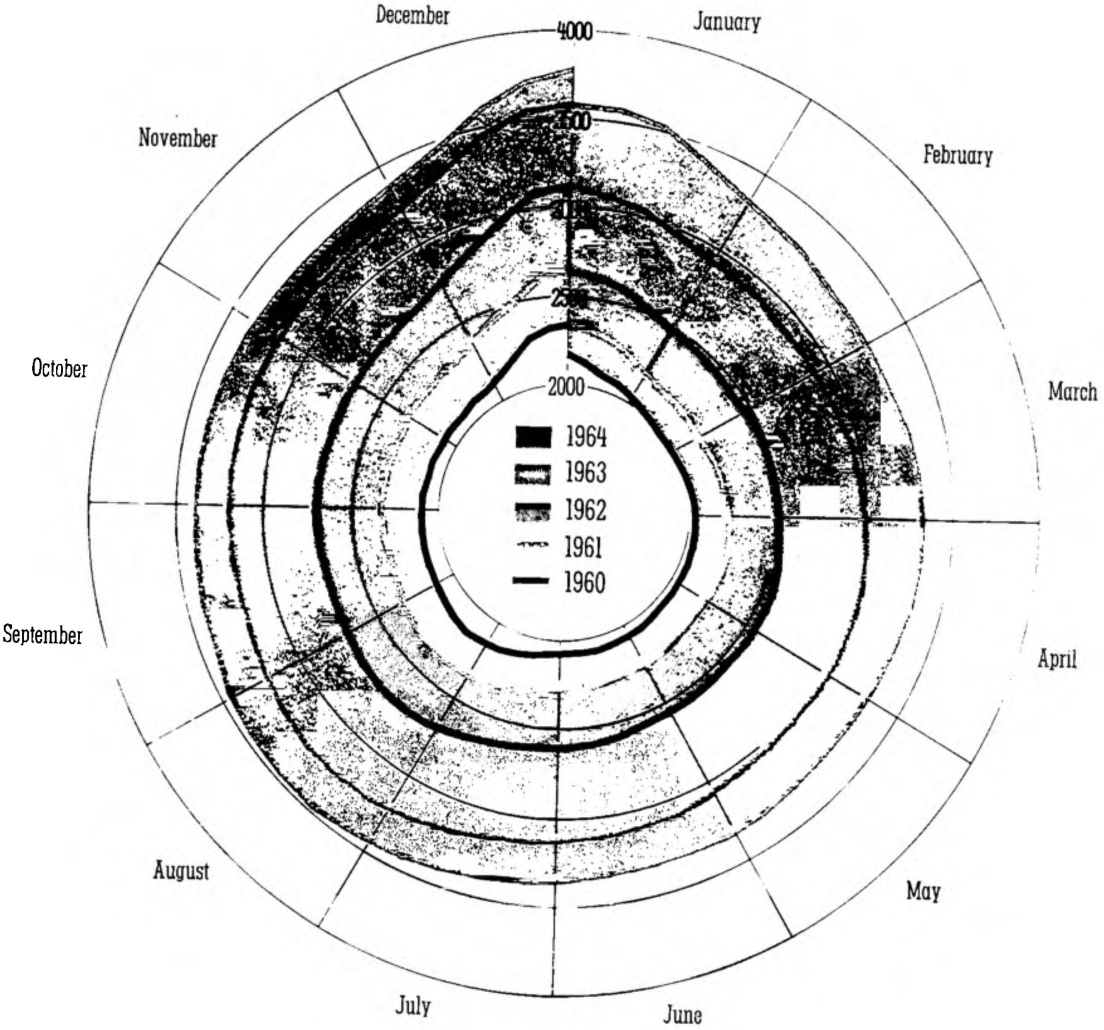
The curve shown in the Chart reflects the trend and also the short-term development of the circulation and conveys an immediate picture of its cyclical movements. The shell of the snail is seen to have begun bulging in 1962, and the margin widened steadily throughout a good part of 1963. It then remained virtually constant between May and the middle of November, and the year-to-year absolute increase eventually began to flatten out and did so more and more throughout 1964, so that the spiral appears to be winding itself more tightly again. The distance between the 1963 and the 1964 curves was smallest during the first week of December; subsequently, the first signs of economic recovery widened the margin again.

Much the same picture emerges if one considers the note and coin circulation net of cash holdings by the Treasury and their percentage variations at twelve-month intervals. The

CHART 15

MONETARY CIRCULATION

(Monthly averages at weekly intervals, in billion lire)



14.2 per cent increment in December 1963 gradually declined to 4.7 per cent in November 1964, and then rose again to 5.9 per cent in December. As a result of this slower rate of increase, the average annual expansion of note and coin circulation was only 8.4 per cent last year, from 3,286.0 to 3,560.8 billion lire.

Since this rate is fairly close to the rate of increase in gross national product at current prices (9.3 per cent), the velocity of circulation in terms of GNP (GNP/circulation) rose again a little after the decreasing tendency of the last few years. The same cannot be said of the ratio either of wage incomes to circulation or of other incomes to circulation; the former continued to go up, the latter down. Once more, the explanation lies in the redistribution of income; there was this difference, however, that in earlier years there was both a wage rise and a shift from independent income earners to wage labour, whereas last year there was a cyclical decline in wage labour.

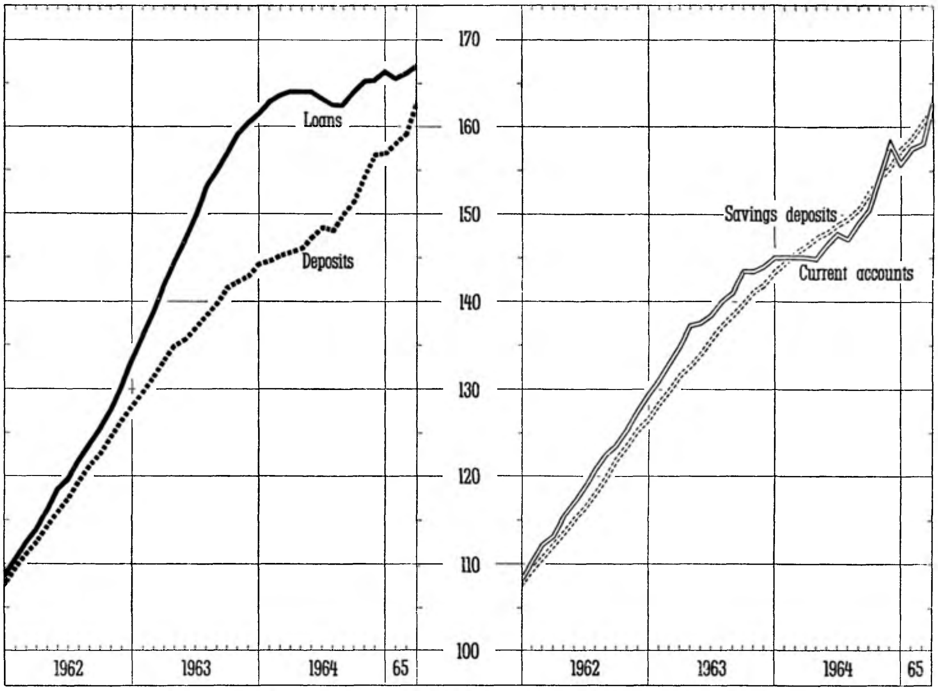
Bank Credits and Deposits.— The salient feature of banking operations last year was that bank credits expanded by a mere 400 billion lire, compared with about 2,300 billion in 1963 and 2,000 billion in 1962.

Ever since 1959 bank credit has been growing fast and almost uninterruptedly for four years, at average annual rates of more than 20 per cent and a peak rate of 25.8 per cent between July 1962 and July 1963. This long and strong expansion abruptly came to a halt in the first few months of 1964 and gave way to almost stationary conditions. Between February 1964 and February 1965 the rate of annual increase dropped from 17.8 to 1.5 per cent.

Seasonally adjusted monthly indices show up three distinct sub-periods during the year; pronounced deceleration in the first quarter, stability and then slight decline between April and August, and finally in the last quarter a gradual upward movement which continued into the early months of 1965 (Chart 16).

In substance, the movement of bank credit as a whole followed short-term lire credits, which increased last year by 227 billion

Chart 16



Loans and deposits of banks and banking associations

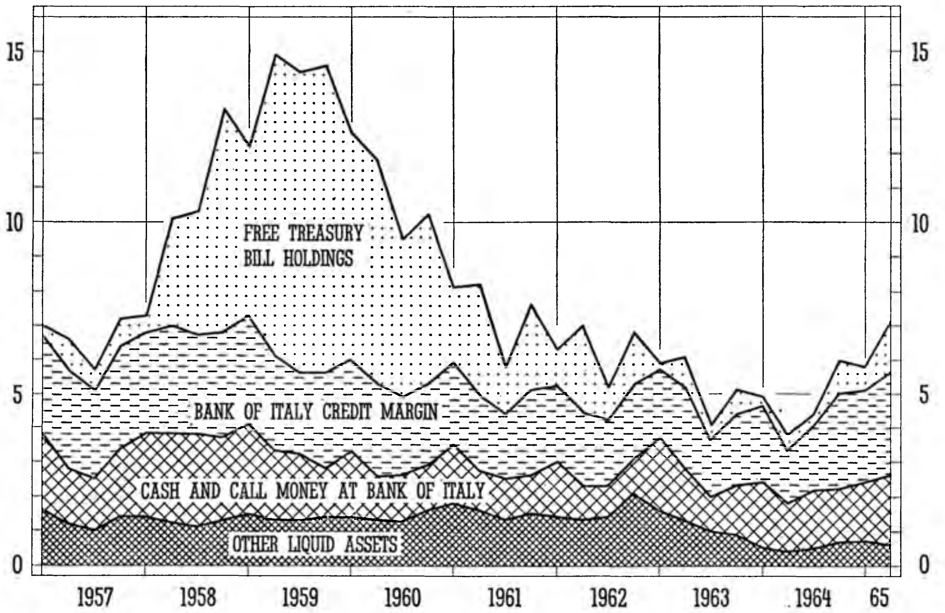
(Seasonally adjusted monthly indices, average 1961 = 100)

lire, or 2.1 per cent, compared with 1,802 billion, or 20.3 per cent, in 1963. Foreign exchange credits to residents declined throughout the first nine months of the year and most sharply between April and July, and then rose again during the last quarter; over the whole year, they fell by 102 billion lire, whereas they had risen by 212 billion in 1963. Medium- and long-term credits merely slowed down their rate of expansion and, in absolute terms, expanded roughly as much as during the preceding year (270 billion, as against 255).

Last year's general slow-down in the expansion of bank credit followed a year of considerable strain when strong credit demand was associated with a very much reduced inflow of deposits. The reasons which pushed up credit demand had to do, in part, with the sluggishness of the capital market, and in part with inflationary pressures which raised the financial requirements of firms and induced business men to borrow in advance of expected restrictions. The rate of expansion of deposits, on the other hand, was held back by income shifts to categories of earners less given to saving, by the growing propensity to consume and the general tight financial position of firms. The big banks also saw both interbank deposits and foreign deposits decline.

The pressure of credit demand on loanable funds was reflected in a rise of the loan/deposit ratio from 75.7 per cent at the end of 1962 to 81.1 per cent at the end of 1963; over the same period, the loan/liabilities ratio rose from 67.1 to 69.1 per cent, and the proportion of funds drawn on open credit lines rose from 72.8 to 76.4 per cent. The banks had to rely heavily on recourse to the central bank during the last quarter of 1963.

Chart 17



Percentage ratio of liquid assets to deposits

Early in 1964 firms were still covering growing financial requirements by drawing more heavily yet on their credit facilities with banks, and the respective ratio is estimated to have climbed above 77 per cent. Over the whole period from August 1963 to March 1964 the banks' liquidity ratio dropped from an already reduced 5.4 per cent to an absolute low point of 3.8 per cent, from which it has since been climbing up slowly (Chart 17).

During the same period, the annual rate of increase in bank credits declined from 25.8 to 16.0 per cent, and the loan/deposit ratio rose from 80.1 to 81.1 per cent.

The events of the second quarter of 1964 had sometimes offsetting and sometimes cumulative effects on banking operations. The general slackening of the pace of economic activity left some firms with larger stocks in hand and therefore with more need for bank credit. Other firms repaid their bank debts, to some extent with the proceeds of exports from stock at the cost of lesser profits. As the pressure on the lira in foreign markets relaxed, some firms found it possible to raise funds directly abroad, both through equity participations and medium- and long-term loans, and part of this money was used to repay bank credits and more particularly overdue prefinancing credits. In the end result, the loan/deposit ratio fell back during these three months to where it had started its rise in August 1963, and the liquidity ratio rose from 3.8 to 4.4 per cent.

In the rather different setting of the second half of last year, when production slowed down, investment stagnated and stocks dwindled, while a large volume of liquidity was being created by the budget deficit and the balance-of-payments surplus, the annual rate of growth of bank credits again dropped, from 9.4 to 3.0 per cent. Similarly, the proportion of credits drawn on existing credit lines fell from 76.4 to 75.1 per cent, and the loan/deposit ratio retreated from 80.0 to 76.8 per cent. The banks' liquidity ratio rose from 4.4 to 5.8 per cent during these six months (from 4.1 to 4.9 per cent in the second half of 1963).

Over the whole of last year the banks' liquid assets increased by 214 billion lire, after a decrease of 52 billion in 1963, and their ratio to deposits improved from 4.9 to 5.8 per cent.

Bank deposits followed a course tendentially parallel to bank credits, except that the downward movement was less and the upward movement more pronounced. Current deposits fluctuated much more sharply than time deposits and so appeared as a much more faithful reflection of the financial difficulties of firms during the first half of the year and the subsequent recovery of company liquidity. Total deposits fell by 69 billion lire during the first half of the year and rose by 1,491 billion during the second half. Their annual rate of increase dropped from 13.0 to 8.6 per cent between December 1963 and June 1964, then went down further to 7.1 per cent at the end of the third quarter, but climbed back to 8.9 per cent by the end of December.

As regards the composition of both bank loans and bank deposits by categories of clients (Tables 37 and 38) as well as the latters' net position vis-à-vis the banking system, there was a reversal of the 1963 disparities between the position of medium and small firms (Other companies, private firms and individuals) and major companies and agencies.

In the system of financial flows between the banks and the economy the smaller businesses, which have a greater propensity to save than to invest, are normally net suppliers of funds to the banks. But in 1963 this category borrowed 1,745 billion lire from the banks and deposited only 1,556 billion (1,322 and 2,083 billion in 1962), so that its net credit position vis-à-vis the banking system was reduced by 189 billion lire. It is interesting to note that simultaneously this same category increased its banknote holdings considerably. Last year the pattern returned to normal with a large excess of 1,569 billion lire of deposits over borrowing, thanks to such general economic factors as a decrease in stocks, more fund-raising on the capital market and smaller cash holdings. In the event, the bank debts of this category of firms and individuals dropped last year by 216 billion lire, and its deposits increased by 1,353 billion.

Major private companies, which normally use part of the liquidity surplus of small and medium-sized firms and especially of households, drew much less new credit last year than in 1963 (129 as against 216 billion lire, or, in relative terms, 11.5 as against 23.8 per cent more). However, some part of this reduction is apparent rather than real, in so far as most electricity companies transferred from the private into the government-controlled sector after nationalization.

The group of government-controlled companies and agencies increased its net indebtedness to the banking system a good deal more than in 1963 (266 as compared with 126 billion lire), partly

TABLE 37

Composition of Bank Loans by Categories of Clients

(billion lire)

Type of bank	Public agencies		Government-controlled companies and agencies (1) (2)		Major private companies (1)		Other companies, private firms and individuals		Total	
	Outstanding at the end of 1964									
Public-law credit institutes	331.4		397.8		319.7		2,124.4		3,173.3	
Banks of national interest	73.6		477.6		473.2		2,114.4		3,138.8	
Ordinary commercial banks	213.3		173.3		254.4		2,178.0		2,819,0	
People's co-operative banks	61.5		39.1		93.7		1,161.1		1,355.4	
Savings banks and pawn banks category I	777.8		88.8		76.9		1,674.5		2,618.0	
Total . . .	1,457.6		1,176.6		1,217.9		9,252.4		13,104.5	
Banking associations	132.3		58.8		31.7		71.5		294.3	
Grand total . . .	1,589.9		1,235.4		1,249.6		9,323.9		13,398.8	
	Absolute increase in									
	1963	1964	1963	1964	1963	1964	1963	1964	1963	1964
Public-law credit institutes	– 18.9	0.9	23.4	79.3	26.1	38.8	522.5	– 62.4	553.1	56.6
Banks of national interest	2.8	14.1	84.0	147.5	114.7	15.5	417.0	–133.2	618.5	43.9
Ordinary commercial banks	0.5	24.7	16.6	36.6	42.1	44.2	335.5	– 36.1	394.7	69.4
People's co-operative banks	6.0	7.5	– 3.8	13.9	2.5	30.9	173.4	– 18.6	178.1	33.7
Savings banks and pawn banks category I	118.7	122.2	45.2	– 3.0	23.2	– 8.2	281.9	34.0	469.0	145.0
Total . . .	109.1	169.4	165.4	274.3	208.6	121.2	1,730.3	–216.3	2,213.4	348.6
Banking associations	20.9	62.0	12.3	– 24.7	7.0	7.7	14.5	0.6	54.7	45.6
Grand total . . .	130.0	231.4	177.7	249.6	215.6	128.9	1,744.8	–215.7	2,268.1	394.2
» » (3) .	*130.0*	*231.4*	*147.5*	*200.9*	*245.8*	*177.6*	*1,744.8*	*–215.7*	*2,268.1*	*394.2*
	Percentage increase in									
	1963	1964	1963	1964	1963	1964	1963	1964	1963	1964
Public-law credit institutes	– 5.4	0.3	7.9	24.9	10.2	13.8	31.4	– 2.9	21.6	1.8
Banks of national interest	4.9	23.7	34.1	44.7	33.4	3.4	22.8	– 5.9	25.0	1.4
Ordinary commercial banks	0.3	13.1	13.9	26.8	25.0	21.0	17.9	– 1.6	16.8	2.5
People's co-operative banks	12.5	13.9	– 13.1	55.2	4.1	49.2	17.2	– 1.6	15.6	2.5
Savings banks and pawn banks category I	22.1	18.6	97.0	– 3.3	37.5	– 9.6	20.7	2.1	23.4	5.9
Total . . .	9.3	13.2	22.4	30.4	23.5	11.1	22.4	– 2.3	21.0	2.7
Banking associations	42.3	88.2	17.3	– 29.6	41.2	32.1	25.7	0.8	28.1	18.3
Grand total . . .	10.6	17.0	22.0	25.3	23.8	11.5	22.4	– 2.3	21.1	3.0
» » (3) .	10.6	17.0	16.6	19.4	29.8	16.6	22.4	– 2.3	21.1	3.0

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(1) Included in the list of 500 companies and agencies with presumed annual sales exceeding 1.5 billion lire.

(2) Including ENEL, the new nationalized electricity board.

(3) This Grand Total differs from the one above because it is calculated on a series which in 1962 and 1963 groups electricity companies not yet taken over by ENEL under government-controlled, rather than under major private, companies.

TABLE 38

Composition of Bank Deposits by Categories of Depositors

(billion lire)

Type of bank	Public agencies	Government-controlled companies and agencies (1) (2)	Major private companies (1)	Other companies, private firms and individuals	Total
	Outstanding at the end of 1964				
Public-law credit institutes	672.4	44.4	138.8	3,072.1	3,927.7
Banks of national interest	234.2	31.4	139.3	2,763.5	3,168.4
Ordinary commercial banks	122.9	14.2	79.0	3,642.3	3,858.4
People's co-operative banks	55.3	2.2	16.9	1,931.8	2,006.2
Savings banks and pawn banks category I	269.7	5.9	29.6	4,135.3	4,440.5
Total . . .	1,354.5	98.1	403.6	15,545.0	17,401.2
Banking associations	10.9	29.4	0.3	9.0	49.6
Grand total . . .	1,365.4	127.5	403.9	15,554.0	17,450.8

Type of bank	Public agencies		Government-controlled companies and agencies (1) (2)		Major private companies (1)		Other companies, private firms and individuals		Total	
	Absolute increase in									
	1963	1964	1963	1964	1963	1964	1963	1964	1963	1964
Public-law credit institutes	217.9	1.8	− 8.2	21.9	− 6.8	11.1	270.0	297.6	472.9	332.4
Banks of national interest	− 9.8	75.3	55.8	− 58.9	1.3	− 12.1	181.2	233.5	228.5	237.8
Ordinary commercial banks	0.3	− 0.6	− 5.5	4.2	2.9	− 6.0	384.0	272.6	381.7	270.2
People's co-operative banks	4.3	1.4	− 1.5	0.5	− 6.7	− 0.8	214.4	148.3	210.5	149.4
Savings banks and pawn banks category I	29.7	13.1	2.5	1.7	2.7	3.8	494.2	405.0	529.1	423.6
Total . . .	242.4	91.0	43.1	− 30.6	− 6.6	− 4.0	1,543.8	1,357.0	1,822.7	1,413.4
Banking associations	3.4	− 1.7	9.2	14.3	..	0.3	11.9	− 4.2	24.5	8.7
Grand total . . .	245.8	89.3	52.3	− 16.3	− 6.6	− 3.7	1,555.7	1,352.8	1,847.2	1,422.1
» » (3) .	*245.8*	*89.3*	*41.4*	*− 23.5*	*4.3*	*3.5*	*1,555.7*	*1,352.8*	*1,847.2*	*1,422.1*
	Percentage increase in									
	1963	1964	1963	1964	1963	1964	1963	1964	1963	1964
Public-law credit institutes	*48.1*	*0.3*	*− 26.7*	*97.3*	*− 5.1*	*8.7*	*10.8*	*10.7*	*15.1*	*9.2*
Banks of national interest	*− 5.8*	*47.4*	*161.7*	*− 65.2*	*0.9*	*− 8.0*	*7.7*	*9.2*	*8.5*	*8.1*
Ordinary commercial banks	*0.2*	*− 0.5*	*− 35.5*	*42.0*	*3.5*	*− 7.1*	*12.9*	*8.1*	*11.9*	*7.5*
People's co-operative banks	*8.7*	*2.6*	*− 46.9*	*29.4*	*27.5*	*− 4.5*	*13.7*	*8.3*	*12.8*	*8.0*
Savings banks and pawn banks category I	*13.1*	*5.1*	*147.1*	*40.5*	*11.7*	*14.7*	*15.3*	*10.9*	*15.2*	*10.5*
Total . . .	*23.7*	*7.2*	*50.4*	*− 23.8*	*− 1.6*	*− 1.0*	*12.2*	*9.6*	*12.9*	*8.8*
Banking associations	*37.0*	*− 13.5*	*155.9*	*94.7*	..	*100.0*	*915.4*	*− 31.8*	*149.4*	*21.3*
Grand total . . .	*23.9*	*7.0*	*57.2*	*− 11.3*	*− 1.6*	*− 0.9*	*12.3*	*9.5*	*13.0*	*8.9*
» » (3) .	*23.9*	*7.0*	*37.8*	*− 15.6*	*1.1*	*0.9*	*12.3*	*9.5*	*13.0*	*8.9*

(1) Included in the list of 500 companies and agencies with presumed annual sales exceeding 1.5 billion lire.

(2) Including ENEL, the new nationalized electricity board.

(3) This Grand Total differs from the one above because it is calculated on a series which in 1962 and 1963 groups electricity companies not yet taken over by ENEL under government-controlled, rather than under major private, companies.

through heavier borrowing (250 as against 178 billion) and partly through a diminution of 16 billion in deposits (as against an increase of 52 billion in 1963).

Finally, public agencies, which had had the benefit of non-banking resources in 1963 and had closed the year with a liquidity surplus of 116 billion lire, last year borrowed 231 billion from the banks, mostly to meet the growing requirements of local authorities.

The Flow of Funds to and from the Banking System.— The net result of the banking system's overall transactions with the above four groups of clients (that is, with the Economy as defined above under the heading The Economy's Liquidity) was that deposits last year exceeded loans by 1,028 billion lire, whereas in 1963 loans had exceeded deposits by 421 billion. Without credits for obligatory stockpiling, the two years' figures rise to 1,043 and 453 billion lire, respectively.

Table 39 shows in detail from what sectors the banking system drew its resources, to what sectors it channelled them, and through what types of operations it did both. Short-term operations are shown separately, and so it can be seen how the liquidity surplus (deficit) was used in (covered by) medium- and long-term operations.

After setting aside the obligatory amounts for reserve deposits and backing for cashiers' cheques (which together tied up 254 billion lire), the banks last year had a residual excess of 789 billion lire of deposits over credits. Of this, 241 billion and 234 billion, respectively, were used to repay debts abroad and to the central bank, and another 200 billion (net of securities earmarked for the compulsory reserve or other operations) to increase the banks' portfolio investments. The rest, together with other funds from various sources, served largely to reconstitute liquid assets (+ 214 billion), especially in the form of free holdings of Treasury Bills and disposable margin with the Bank of Italy (including 52 billion repayments on the latter). As regards relations with other sectors, banks and banking associations last year became net debtors to the Economy to the

TABLE 39

Assets and Liabilities of Banks and Banking Associations

(changes in billion lire; italic figures denote liabilities)

Items	Goverment and Central Post Office Savings Fund		Bank of Italy and Italian Exchange Office		Banks		Special Credit Institutes		Economy		Total	
	1963	1964	1963	1964	1963	1964	1963	1964	1963	1964	1963	1964
CASH	—	—	32.3	– 44.2	—	—	—	—	—	—	32.3	– 44.2
DEPOSITS IN CURRENT ACCOUNT												
Disposable credit margin with Bank of Italy	—	—	66.6	112.8	—	—	—	—	—	—	66.6	112.8
Others by banks	2.0	10.5	– 35.0	37.4	–117.4	495.6	– 33.3	5.0	—	—	–183.7	548.5
Others at banks	—	—	—	—	*–117.4*	*495.6*	*61.8*	*42.0*	*834.6*	*584.5*	*779.0*	*1,122.3*
OTHER DEPOSITS												
for compulsory reserves (1)	—	—	322.1	151.9	—	—	—	—	—	—	322.1	151.9
others by banks	—	—	—	—	– 72.2	92.4	—	—	—	—	– 72.2	92.4
others at banks	—	—	—	—	*– 72.2*	*92.4*	*9.5*	*– 2.6*	*1,012.6*	*837.6*	*949.9*	*927.4*
TREASURY BILLS												
free holdings	23.6	67.4	—	—	—	—	—	—	—	—	23.6	67.4
earmarked for compulsory reserves (1)	– 14.5	– 25.6	—	—	—	—	—	—	—	—	– 14.5	– 25.6
earmarked as collateral for advances	– 14.1	– 12.4	—	—	—	—	—	—	—	—	– 14.1	– 12.4
earmarked as collateral for other operations	– 8.8	54.3	—	—	—	—	—	—	—	—	– 8.8	54.3
Total	– 13.8	83.7	—	—	—	—	—	—	—	—	– 13.8	83.7
SHORT-TERM CREDITS												
Lire:												
Credit line with Bank of Italy												
advances drawn	—	—	*77.6*	*– 52.0*	—	—	—	—	—	—	*77.6*	*– 52.0*
disposable margin	—	—	*66.6*	*112.8*	—	—	—	—	—	—	*66.6*	*112.8*
Stockpiling bills not rediscounted	– 35.8	5.2	—	—	—	—	—	—	—	—	– 35.8	5.2
Trade bills	—	—	—	—	—	—	—	—	755.0	131.2	755.0	131.2
Trade bills rediscounted	—	—	*289.0*	*–200.9*	—	—	—	—	—	—	*289.0*	*–200.9*
Credits in current account:												
stockpiling credits	– 40.1	– 10.6	—	—	—	—	—	—	—	—	– 40.1	– 10.6
ordinary overdrafts to clients	—	—	—	—	—	—	—	—	1,024.6	126.6	1,024.6	126.6
Contangoes and advances to clients on securities	—	—	—	—	—	—	—	—	50.9	– 51.6	50.9	– 51.6
Other short-term credits extended	—	—	—	—	8.8	– 6.9	—	—	2.9	4.7	11.7	– 2.2
Other short-term credits received	—	—	*30.1*	*9.0*	*8.8*	*– 6.9*	—	—	—	—	*38.9*	*2.1*
Foreign exchange credits to residents	—	—	—	—	—	—	—	—	211.5	–101.7	211.5	–101.7
Foreign exchange debts to residents	—	—	*– 10.2*	*9.9*	—	—	—	—	—	—	*– 10.2*	*9.9*
Total	– 75.9	– 5.4	—	—	8.8	– 6.9	—	—	2,044.9	109.2	1,977.8	96.9
Total	—	—	*453.1*	*–121.2*	*8.8*	*– 6.9*	—	—	—	—	*461.9*	*–128.1*
MEDIUM- AND LONG-TERM CREDITS	—	—	—	—	—	—	46.0	65.5	254.8	269.5	300.8	335.0
BONDS												
free holdings	– 82.9	– 19.1	—	—	—	—	54.0	69.5	18.6	149.7	– 10.3	200.1
earmarked:												
for compulsory reserves (1)	– 1.6	– 6.3	—	—	—	—	126.2	15.3	—	119.0	124.6	128.0
as collateral for advances	40.5	– 2.2	—	—	—	—	140.9	82.9	33.1	16.9	214.5	97.6
as collateral for other operations	7.7	24.6	—	—	—	—	– 13.6	15.8	18.8	– 8.0	12.9	32.4
Total	– 36.3	– 3.0	—	—	—	—	307.5	183.5	70.5	277.6	341.7	458.1
SHARES AND EQUITY PARTICIPATIONS												
Free holdings	—	—	—	—	—	—	—	—	– 68.0	– 20.4	– 68.0	– 20.4
Others	—	—	—	—	—	—	27.9	13.6	9.6	– 4.6	37.5	9.0
Total	—	—	—	—	—	—	27.9	13.6	– 58.4	– 25.0	– 30.5	– 11.4
OTHER ASSETS AND LIABILITIES	—	—	—	—	—	—	—	—	*144.2*	*178.5*	*144.2*	*178.5*
POSITION VIS-A-VIS ABROAD												
Convertible currencies (free holdings)	—	—	—	—	—	—	—	—	—	—	– 65.6	35.5
Other foreign assets	—	—	—	—	—	—	—	—	—	—	– 42.8	61.2
Other foreign liabilities	—	—	—	—	—	—	—	—	—	—	*297.7*	*–179.7*
Total	—	—	—	—	—	—	—	—	—	—	*406.1*	276.4
Total assets (2)	–124.0	85.8	386.0	257.9	–180.8	581.1	348.1	267.6	2,311.8	631.3	2,632.7	1,920.4
Total liabilities (2)	—	—	*453.1*	*–121.2*	*–180.8*	*580.1*	*71.3*	*39.6*	*1,991.4*	*1,600.6*	*2,632.7*	*1,920.4*
Balance (3)	*124.0*	85.8	*67.1*	379.1	—	—	276.8	228.0	320.4	*969.3*	—	—

(1) Including backing for cashiers' cheques.

(2) Including position vis-à-vis abroad.

(3) Italics denote net deficit.

extent of 969 billion dollars, in contrast to their net lending of 320 billion to the Economy in 1963. The excess funds were used in operations with the foreign sector (276 billion), the Treasury (86 billion), the central bank (379 billion) and special credit institutes (288 billion).

Among operations with the central bank, it is interesting to note that the banks presented 200 billion lire less of bills for rediscount, the ordinary bill portfolio itself having risen only by a very moderate amount; in 1963, the ordinary bill portfolio had increased by as much as 755 billion, and 289 billion of it had been rediscounted.

The Central Risk Pool.— The new central risk pool which the Joint Ministerial Committee on Credit and Saving, by a decision of 16 May 1962, asked the Bank of Italy to establish, began to work last year. In January, instructions went out to all registered banks and banking associations to the effect that bank branches were to start filing their monthly reports in March, and since then 14 such monthly reports have been processed. Bank branches notified the pool of some 200,000 credits extended, and received from the pool about as many statements on clients' total credit positions. More than one quarter of the statements were sent by means of automatic electronic supports and it is hoped to increase this proportion in 1965.

The lower limit of notifiable credits was lowered from 250 to 100 million lire in February of this year, and the system is now being extended also to the whole sector of special credit institutes.

Quite apart from its strictly operational uses, the material processed by the risk pool has added much to our knowledge of the banking system's lending activities. New and original information shed a good deal of light on phenomena whose real magnitude could formerly only be guessed at. The most important results of the pool's statistical elaborations were communicated from time to time to member banks for purposes of comparison with their own corresponding business figures and consequent better control over the quantity and quality of credits; more generally speaking, the dissemination of knowledge ought to help the pool to do one of the things which it was set up to do, namely, to reinforce safeguards apt to forestall any aggravation of credit risks.

The pool's activities since its inception to the end of March 1965 are summarized in Table 40. It will be seen that both the number and the value of the credit risks evaluated have been growing steadily.

TABLE 40

The Central Risk Pool's Evaluations of Credits Extended and Used

(End-quarter figures)

Items	1964 (1)				1965	
	March	June	Sept.	Dec.	March (1)	March (2)
1. Number of clients evaluated	4,306	4,253	4,289	4,468	4,708	12,247
2. Number of (partial) credits notified	9,990	10,194	10,475	11,048	11,183	27,884
3. Average number of separate credits per client (2:1)	2.30	2.39	2.44	2.47	2.37	2.28
4. Total value of credits evaluated (billion lire):						
a) credits extended	8,642	9,070	9,328	9,948	10,520	12,969
b) credits used	6,353	6,712	6,759	7,218	7,222	8,829
Degree of credit utilization (per cent)	*73.5*	*74.0*	*72.4*	*72.5*	*68.6*	*68.0*
5. Average amount of credit per client evaluated (million lire):						
a) credits extended	2,700	2,133	2,175	2,226	2,234	1,059
b) credits used	1,475	1,578	1,576	1,615	1,534	721

(1) Above 250 million lire per credit notified.
(2) Above 100 million lire per credit notified.

The figures of the amount of credit risks notified to the pool by December 1964 together with those of the banks' own quarterly position show that altogether about 45 per cent of all credits were covered by the pool's evaluations. Within this overall figure there are marked disparities according to types of banks and types of credit, because of the difference in credit composition as among various parts of our banking system.

Now that the lower limit of notifiable credits has been brought down, the proportion of credit risks covered has risen to 55 per cent of the total.

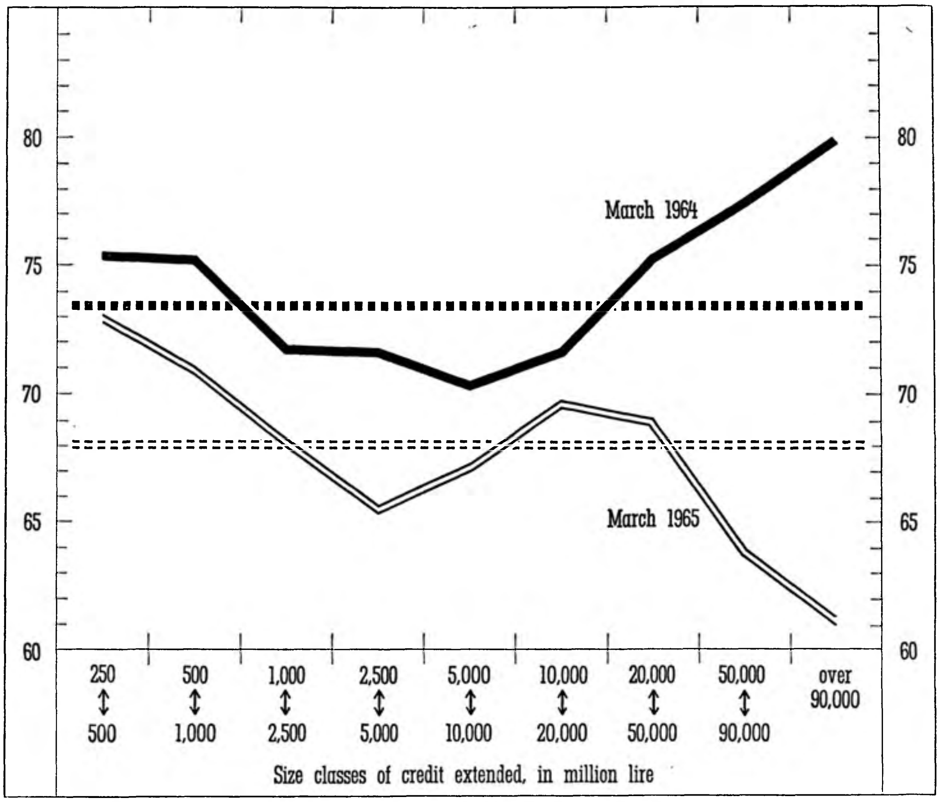
To probe more deeply into some aspects of particular relevance to the pool's work, detailed studies were made of the figures relating to certain months of 1964, when the 250-million limit was still in force, and in 1965, with the new 100-million limit. One of the things which an attempt was made to find out was what bearing the amount of bank credit extended to any one client or, from the other side, the unit size of borrowing firms, has on the practice of risk-sharing among several banks and on the degree of utilization of credit lines. It appeared that the big borrowers were also those who used the largest number of separate credit facilities. The explanation of the very marked fractionalization of the credit risk at the highest levels of credit distribution lies in a variety of different factors, including the banks' own practices of risk evaluation, competition among banks, the legal ceiling on credits, and the greater wealth of information available on this class of credit users. Immediately below the top level of the amount of total credit outstanding to any one client, the number of banks which share one credit risk tends to be much smaller, but still rather high.

In each size class of total credit extended to any one client, the average number of risk-sharing banks is invariably smaller than in the same size class of credit used. The reason is that it is normal practice not to draw the whole of any credit line. Generally speaking, the lag between the two distributions fluctuates closely around the average utilization ratio, but considerable differences are observed as between successive size classes in connection with the different degree of credit utilization prevalent in them. Actually, the degree of credit utilization was seen to vary not only with the unit amount of credit, that is, with the size of the borrowing firm, but also over time.

Over the course of 1964, fairly similar developments in the various credit groups and branches of economic activity showed an overall tendency for the value of credits extended to grow faster than the value of credits used. This is confirmed by a reduction of the overall degree of credit utilization from 73.5

to 68 per cent between March 1964 and March 1965; the drop was more pronounced in the higher size classes (over 10 billion), which, in March 1964, generally displayed an above-average degree of credit utilization in sharp contrast to the situation at present (Chart 18).

CHART 18



Percentage utilization of credits evaluated, by size classes of total credit extended per client

VIII. *The Economy's Total Supply and Use of Funds*

The Supply of Funds: The Credit System and the Capital Market.— The total supply of funds reaching the Economy in 1964 amounted to 3,225 billion lire. This was about one third less than in the preceding year.

The contraction was entirely attributable to short-term credits, which dwindled from 2,098 billion to a mere 124 billion lire; medium- and long-term loans together with subscriptions to bonds and shares rose from 2,603 to 3,101 billion lire.

Of the total of 3,225 billion lire, local authorities and public agencies absorbed 1,145 billion and government-controlled companies another 1,085 billion. Thus the public sector of the Economy received 69 per cent of the total supply of resources; in 1963 the proportion was only 33 per cent.

Both in 1962 and in 1963 short-term bank credits had helped to finance investment expenditure to the extent that the capital market failed to do so; the year 1964 saw a return to forms of finance more evenly matched with the duration of its use, and the deceleration of the expansion of short-term bank credits to some extent reflects the repayment of earlier prefinancing credits.

The flow of medium- and long-term credits expanded by much the same amount in the last two years, but while in 1963 the increment came in substance from the banks and the Central Post Office Savings Fund, the latter, together with Social Insurance Funds, was almost alone responsible for last year's increment. In both years, but more especially so in 1964, conspicuous net inflows of medium- and long-term loans came from abroad, either directly to firms or through banks and special credit institutes.

Bond issues furnished the Economy with 507 billion lire last year (369 billion in 1963), thanks in good part to subscriptions by banks.

The funds supplied by share issues were, at 575 billion lire, somewhat more plentiful than in 1963 (433 billion), but still far short of the 777 billion of 1962. Of a total inflow of 334 billion lire in the form of direct foreign investment, 169 billion were share subscriptions (31 out of a total of 206 billion in 1963).

The Use of Funds: Public and Private Investment.— Public investment expenditure was almost identical in the last two years, though there are considerable internal differences. Government investment declined sharply, mostly thanks to lower outgoings to the industrial sector, and the Cassa per il Mezzogiorno spent slightly less. All other public investment expenditures were up on the preceding year, and most spectacularly so those of autonomous government agencies (mostly for fixed railway installations) and of the Central Post Office Savings Fund (more bond subscriptions). Expenditure on low-cost housing by the Worker's Housing Agency GESCAL were fairly low, as were those of its predecessor INA-Casa in 1963 (Table 41).

Table 41

Public Investment Expenditure

(billion lire)

Investment by	1963	1964
Government	852	637
Local authorities	399	442
Autonomous government agencies	127	253
Cassa per il Mezzogiorno	248	222
Central Post Office Savings Fund	253	308
GESCAL (formerly INA-Casa)	31	33
Total . . .	1,910	1,895

Similarly, the sources of finance for public investment were rather different in the two last years. The salient feature last year was that a shortfall in public saving had to be made good by heavier borrowing—in an amount of 1,199 billion lire last year, compared with 1,040 billion in 1963 (Table 42).

Table 42

Recapitulation of Sources of Investment Finance

(billion lire)

Sources of investment funds	Public investment		Private investment		Total investment	
	1963	1964	1963	1964	1963	1064
Medium- and long-term credit	— 104	239	1,496	1,859	1,392	2,098
Net short-term credit	1,144	960	1,617	971	3,489	2,540
Self-financing (1)	728	609				
Direct investment by individuals	—	—				
Depreciation reserves	—	—	1,843	1,950	1,843	1,950
Other sources	142	87	—	—	142	87
Total . . .	1,910	1,895	4,956	4,780	6,866	6,675

(1) In Public Administration, self-financing is equated with current surplus.

As regards the sources of finance for private investment, three features stand out in the comparison between the last two years: (a) more claims were made last year on medium- and long-term credit, especially in the form of security issues; (b) depreciation reserves furnished much the same resources in both years; (c) there was a sharp fall in the balancing item which includes direct investment by individuals, self-financing by companies and the net balance of operations with banks. This fall is probably the resultant of a contraction in the last two components of the balancing item (in the case of operations with banks this presumption is confirmed by the change in the loan/deposit ratio) and some increase in the first, namely, direct investment by individuals (some confirmation can here be deduced from the volume of funds estimated to have been spent for the purchase of houses or flats).

Tabulation of Financial Flows.— A determined effort has been made in the Annual Report this year to identify the flows of financial assets from, to and through the country's financial enterprises, or rather homogeneous groups of them. An attempt at overall tabulation of all these figures in a sort of National Financial Accounts has been made in Table 43.

It is only right to stress the tentative nature of this construction. There is as yet no consensus of opinion about the contents of such accounts, but this first attempt in Italy follows the line adopted by other countries, and more particularly by the European Economic Community in its work on a joint schedule of economic and financial national accounts.

Table 43

National Financial Assets and Liabilities

(changes in billion lire)

Assets transferred and *liabilities* contracted by sectors / towards counterpart sectors	1963														1964													
	Households and non-financial enterprises	Financial enterprises				Treasury			Foreign Sector	Unclassifiable and discrepancies	Total				Households and non-financial enterprises	Financial enterprises				Treasury			Foreign Sector	Unclassifiable and discrepancies	Total			
		Bank of Italy and Ital. Exch. Office	Banks	Special credit institutes	Insurance companies	Government	Central Post Office Savings Fund	Social Insurance Funds			assets	liab.	balance			Bank of Italy and Ital. Exch. Office	Banks	Special credit institutes	Insurance companies	Government	Central Post Office Savings Fund	Social Insurance Funds			assets	liab.	balance	
HOUSEHOLDS AND NON-FINANCIAL ENTERPRISES																												
a) Notes and coin	—	432.4	—	—	—	8.5	—	—	—	—	440.9	—	440.9	a)	—	259.6	—	—	—	11.0	—	—	—	—	270.6	—	270.6	a)
b) Sight deposits	—	9.9	647.2	—	—	—	82.1	—	—	1.0	740.2	—	740.2	b)	—	–8.5	446.6	—	—	—	19.9	—	—	44.2	502.2	—	502.2	b)
c) Other deposits	—	—	1,031.7	—	—	—	339.7	—	—	—	1,371.4	—	1,371.4	c)	—	—	871.7	—	—	—	300.6	—	—	—	1,172.3	—	1,172.3	c)
d) Short-term securities	—	—	—	—	—	–117.7	—	—	—	—	–117.7	—	–117.7	d)	—	—	—	—	—	–11.6	—	—	—	—	–11.6	—	–11.6	d)
e) Short-term credits	—	–1.7	2,044.9	54.6	—	—	—	—	—	—	—	2,097.8	2,097.8	e)	—	–0.3	109.2	15.5	—	—	—	—	—	—	—	124.4	124.4	e)
f) Medium- and long-term credits	—	—	—	—	—	—	—	—	14.4	8.5	22.9	—	22.9	f)	—	—	—	—	—	—	—	—	30.9	16.2	47.1	—	47.1	f)
Medium- and long-term credits	—	—	255.6	956.3	17.3	14.4	351.2	32.3	173.6	—	—	1,800.7	1,800.7		—	—	254.5	932.7	20.7	1.8	452.0	100.6	256.4	—	—	2,018.7	2,018.7	
g) Bonds	135.0	—	—	336.9	—	–162.0	—	—	11.0	—	320.9	—	320.9	g)	53.3	—	—	178.0	—	52.0	—	—	—	—	283.3	—	283.3	g)
Bonds	135.0	5.5	70.5	5.0	4.0	—	137.4	8.9	2.9	—	—	369.2	369.2		53.3	–0.4	277.6	6.6	1.9	—	104.7	57.3	5.9	—	—	506.9	506.9	
h) Shares and equity participations	–141.6	—	2.5	1.6	1.0	—	—	—	34.7	—	–101.8	—	–101.8	h)	253.7	—	6.7	..	1.1	—	—	—	36.2	—	297.7	—	297.7	h)
Shares and equity participations	–141.6	—	–58.4	–0.2	11.3	47.0	—	4.9	569.6	—	—	432.6	432.6		253.7	—	–25.0	4.3	7.3	25.0	—	—	309.9	—	—	575.2	575.2	
i) Other financial assets and *liabilities*	—	—	—	155.5	119.1	—	6.6	173.0	913.8	116.0	1,484.0	—	1,484.0	i)	—	—	—	40.3	123.8	—	7.6	206.0	343.3	140.7	861.7	—	861.7	i)
Net financial surplus or *deficit*	=	438.5	631.2	521.7	87.5	332.6	60.2	126.9	227.8	125.5	4,160.8	4,700.3	539.5		=	251.8	708.7	740.8	95.0	24.6	228.6	48.1	161.8	201.1	3,423.3	3,225.2	198.1	
FINANCIAL ENTERPRISES																												
Bank of Italy and Italian Exchange Office																												
A) Gold	—	—	—	—	—	—	—	—	62.3	—	62.3	—	62.3	A)	—	—	—	—	—	—	—	—	–147.8	—	–147.8	—	–147.8	A)
a) Notes and coin	—	—	—	—	—	–2.7	—	—	..	—	–2.7	—	–2.7	a)	—	—	—	—	—	–2.6	—	—	..	—	–2.6	—	–2.6	a)
Notes and coin	432.4	—	32.3	..	—	–0.5	....	—	—	—	—	464.2	464.2		259.6	—	–44.2	..	—	0.1	....	—	—	—	—	215.5	215.5	
b) Sight deposits	—	—	—	—	—	15.4	—	—	—	—	15.4	—	15.4	b)	—	—	—	—	—	–0.6	—	—	—	—	–0.6	—	–0.6	b)
Sight deposits	9.9	—	31.6	3.1	—	–320.3	—	7.6	81.7	—	—	–186.4	–186.4		–8.5	—	150.2	13.1	—	—	—	–6.3	–79.6	—	—	68.9	68.9	
c) Other deposits	—	—	322.1	—	—	–8.8	—	—	10.4	—	—	323.7	323.7	c)	—	—	151.9	—	—	–9.7	—	—	–10.4	—	—	131.8	131.8	c)
Other deposits	—	—	—	—	—	—	—	—	–4.2	—	–4.2	—	–4.2		—	—	—	—	—	—	—	—	–4.7	—	–4.7	—	–4.7	
d) Short-term securities	—	—	—	—	—	–54.6	—	—	–336.8	—	–391.4	—	–391.4	d)	—	—	—	—	—	160.0	—	—	480.8	—	640.8	—	640.8	d)
e) Short-term credits	–1.7	—	453.1	18.4	—	459.7	—	—	–12.2	—	917.3	—	917.3	e)	–0.3	—	–121.2	4.3	—	64.8	—	—	–67.2	—	–119.6	—	–119.6	e)
f) Medium- and long-term credits	—	—	—	—	—	28.6	—	—	–6.0	—	22.6	—	22.6	f)	—	—	—	—	—	26.1	—	—	–13.9	—	12.2	—	12.2	f)
Medium- and long-term credits	—	—	—	—	—	—	—	—	0.8	—	—	0.8	0.8		—	—	—	—	—	—	—	—	–0.6	—	—	–0.6	–0.6	
g) Bonds	5.5	—	—	–0.4	—	–8.8	—	—	15.3	—	11.6	—	11.6	g)	–0.4	—	—	10.3	—	168.4	—	—	–130.3	—	48.0	—	48.0	g)
i) Other financial assets and *liabilities*	—	—	—	—	—	—	—	—	—	28.6	—	28.6	28.6	i)	—	—	—	—	—	—	—	—	—	10.1	—	10.1	10.1	i)
Net financial surplus or *deficit*	438.5	—	67.1	14.9	—	767.2	—	7.6	374.5	28.6	630.9	630.9	=		251.8	—	379.1	1.5	—	425.7	—	6.3	207.5	10.1	425.7	425.7	=	
Banks																												
a) Notes and coin	—	32.3	—	—	—	—	—	—	1.3	—	33.6	—	33.6	a)	—	–44.2	—	—	—	—	—	—	0.1	—	–44.1	—	–44.1	a)
b) Sight deposits	—	31.6	–117.4	–33.3	—	–0.3	2.3	—	40.8	–1.0	–77.3	—	–77.3	b)	—	150.2	495.6	5.0	—	9.4	1.1	—	–24.9	–44.2	592.2	—	592.2	b)
Sight deposits	647.2	—	–117.4	61.8	7.3	—	—	204.1	275.6	—	—	1,078.6	1,078.6		446.6	—	495.6	42.2	18.9	—	—	109.7	–184.7	—	—	928.3	928.3	
c) Other deposits	—	322.1	–72.2	—	—	—	—	—	–168.5	—	81.4	—	81.4	c)	—	151.9	92.4	—	—	—	—	—	124.6	—	368.9	—	368.9	c)
Other deposits	1,031.7	—	–72.2	9.5	—	—	—	—	—	—	—	969.0	969.0		871.7	—	92.4	–2.6	—	—	—	—	—	—	—	961.5	961.5	
d) Short-term securities	—	—	—	—	—	–13.8	—	—	—	—	–13.8	—	–13.8	d)	—	—	—	—	—	83.7	—	—	—	—	83.7	—	83.7	d)
e) Short-term credits	2,044.9	—	8.8	—	—	–75.9	—	—	18.0	—	1,995.8	—	1,995.8	e)	109.2	—	–6.9	—	—	–5.4	—	—	4.8	—	101.7	—	101.7	e)
Short-term credits	—	453.1	8.8	—	—	—	—	—	25.5	—	—	487.4	487.4		—	–121.2	–6.9	—	—	—	—	—	5.0	—	—	–123.1	–123.1	
f) Medium- and long-term credits	255.6	—	—	46.0	–0.8	—	—	—	—	—	300.8	—	300.8	f)	254.5	—	—	65.5	15.0	—	—	—	—	—	335.0	—	335.0	f)
g) Bonds	70.5	—	—	307.5	—	–36.3	—	—	—	—	341.7	—	341.7	g)	277.6	—	—	183.4	—	–3,0	—	—	—	—	458.0	—	458.0	g)
h) Shares and equity participations	–58.4	—	—	27.9	—	—	—	—	—	—	–30.5	—	–30.5	h)	–25.0	—	—	10.7	—	—	—	—	—	—	–14.3	—	–14.3	h)
Shares and equity participations	2.5	—	—	—	—	—	—	—	—	—	—	2.5	2.5		6.7	—	—	—	—	—	—	—	—	—	—	6.7	6.7	
i) Other financial assets and *liabilities*	—	—	—	—	—	—	—	—	–3.4	97.6	—	94.2	94.2	i)	—	—	—	—	—	—	—	—	7.9	99.8	—	107.7	107.7	i)
Net financial surplus or *deficit*	631.2	67.1	=	276.8	8.1	126.3	2.3	204.1	406.1	98.6	2,631.7	2,631.7	=		708.7	379.1	=	225.0	3.9	84.7	1.1	109.7	276.4	144.0	1,881.1	1,881.1	=	
Special Credit Institutes																												
b) Sight deposits	—	3.1	61.8	—	—	—	..	—	—	—	64.9	—	64.9	b)	—	13.1	42.2	—	—	—	–0.2	—	—	—	55.1	—	55.1	b)
Sight deposits	—	—	–33.3	—	—	—	—	—	—	—	—	–33.3	–33.3		—	—	5.0	—	—	—	—	—	—	—	—	5.0	5.0	
c) Other deposits	—	—	9.5	—	—	—	—	—	—	—	9.5	—	9.5	c)	—	—	–2.6	—	—	—	—	—	—	—	–2.6	—	–2.6	c)
e) Short-term credits	54.6	18.4	—	—	—	–11.1	—	—	—	—	43.5	18.4	25.1	e)	15.5	4.3	—	—	—	27.4	—	—	—	—	42.9	4.3	38.6	e)
f) Medium- and long-term credits	956.3	—	—	—	—	—	—	—	26.0	—	982.3	—	982.3	f)	932.7	—	—	—	—	—	—	—	4.5	—	937.2	—	937.2	f)
Medium- and long-term credits	—	—	46.0	—	—	42.8	—	15.0	38.5	8.5	—	150.8	150.8		—	—	65.5	—	—	28.4	—	2.5	126.1	16.2	—	238.7	238.7	
g) Bonds	5.0	—	—	..	—	–0.5	—	—	—	—	4.5	—	4.5	g)	6.6	—	—	5.1	—	0.5	—	—	—	—	12.2	—	12.2	g)
Bonds	336.9	–0.4	307.5	..	18.8	—	53.1	58.8	—	—	—	774.7	774.7		178.0	10.3	183.4	5.1	12.8	—	151.7	173.1	—	—	—	714.4	714.4	
h) Shares and equity participations	–0.2	—	—	1.4	—	—	—	—	—	—	1.2	—	1.2	h)	4.3	—	—	..	—	—	—	—	—	—	4.3	—	4.3	h)
Shares and equity participations	1.6	—	27.9	1.4	4.1	16.5	1.5	—	—	—	—	53.0	53.0		..	—	10.7	..	1.4	5.3	0.2	—	—	—	—	17.6	17.6	
i) Other financial assets and *liabilities*	155.5	—	—	—	—	—	—	—	—	13.2	13.2	155.5	142.3	i)	40.3	—	—	—	—	—	—	—	—	28.8	—	69.1	69.1	i)
Net financial surplus or *deficit*	521.7	14.9	276.8	=	22.9	70.9	54.6	73.8	12.5	4.7	1,119.1	1,119.1	=		740.8	1.5	225.0	=	14.2	5.8	152.1	175.6	121.6	45.0	1,049.1	1,049.1	=	
Insurance companies																												
b) Sight deposits	—	—	7.3	—	—	—	—	—	—	—	7.3	—	7.3	b)	—	—	18.9	—	—	—	—	—	—	—	18.9	—	18.9	b)
f) Medium- and long-term credits	17.3	—	–0.8	—	—	—	—	—	—	—	17.3	–0.8	18.1	f)	20.7	—	15.0	—	—	—	—	—	—	—	20.7	15.0	5.7	f)
g) Bonds	4.0	—	—	18.8	—	–2.1	—	—	—	—	20.7	—	20.7	g)	1.9	—	—	12.8	—	..	—	—	—	—	14.7	—	14.7	g)
h) Shares and equity participations	11.3	—	—	4.1	—	—	—	—	12.9	—	28.3	—	28.3	h)	7.3	—	—	1.4	—	—	—	—	13.9	—	22.6	—	22.6	h)
Shares and equity participations	1.0	—	—	—	—	—	—	—	—	—	—	1.0	1.0		1.1	—	—	—	—	—	—	..	—	—	—	1.1	1.1	
i) Other financial assets and *liabilities*	119.1	—	—	—	—	—	—	—	6.5	—	—	125.6	125.6	i)	123.8	—	—	—	—	—	—	—	6.6	—	—	130.4	130.4	i)
Net financial surplus or *deficit*	87.5	—	8.1	22.9	—	2.1	—	—	6.4	—	73.6	125.8	52.2		95.0	—	3.9	14.2	—	—	—	—	7.3	—	76.9	146.5	69.6	
TREASURY																												
Government																												
a) Notes and coin	—	–0.5	—	—	—	—	—	—	—	—	–0.5	—	–0.5	a)	—	0.1	—	—	—	—	—	—	—	—	0.1	—	0.1	a)
Notes and coin	8.5	–2.7	—	—	—	—	—	—	—	—	—	5.8	5.8		11.0	–2.6	—	—	—	—	—	—	—	—	—	8.4	8.4	
b) Sight deposits	—	–320.3	—	—	—	—	—	—	—	—	–320.3	—	–320.3	b)	—	—	—	—	—	—	—	—	—	—	—	—	—	b)
Sight deposits	—	15.4	–0.3	—	—	—	—	—	—	—	—	15.1	15.1		—	–0.6	9.4	—	—	—	—	—	—	—	—	8.8	8.8	
c) Other deposits	—	–8.8	—	—	—	—	–256.4	6.8	—	—	–8.8	–249.6	–240.8	c)	—	–9.7	—	—	—	—	–372.0	–8.3	—	—	–9.7	–380.3	–370.6	c)
d) Short-term securities	–117.7	–54.6	–13.8	—	—	—	—	—	—	—	—	–186.1	–186.1	d)	–11.6	160.0	83.7	—	—	—	—	—	—	—	—	232.1	232.1	d)
e) Short-term credits	—	459.7	–75.9	–11.1	—	—	—	—	—	—	—	372.7	372.7	e)	—	64.8	–5.4	27.4	—	—	—	—	—	—	—	86.8	86.8	e)
f) Medium- and long-term credits	14.4	28.6	—	42.8	—	—	—	—	—	—	57.2	28.6	28.6	f)	1.8	26.1	—	28.4	—	—	—	—	—	—	30.2	26.1	4.1	f)
g) Bonds	–162.0	–8.8	–36.3	–0.5	–2.1	—	143.9	–5.0	—	—	—	–70.8	–70.8	g)	52.0	168.4	–3.0	0.5	—	—	–7.6	–0.7	—	—	—	209.6	209.6	g)
h) Shares and equity participations	47.0	—	—	16.5	—	—	—	—	—	—	63.5	—	63.5	h)	25.0	—	—	5.3	—	—	—	—	—	—	30.3	—	30.3	h)
i) Other financial assets and *liabilities*	—	—	—	—	—	—	—	1.3	—	—	—	1.3	1.3	i)	—	—	—	—	—	—	—	–4.6	—	—	—	–4.6	–4.6	i)
Net financial surplus or *deficit*	332.6	767.2	126.3	70.9	2.1	—	112.5	3.1	—	—	–208.9	–83.0	125.9		24.6	425.7	84.7	5.8	—	—	379.6	13.6	—	—	50.9	186.9	136.0	
Central Post Office Savings Fund																												
b) Sight deposits	82.1	—	2.3	..	—	—	—	—	—	—	—	84.4	84.4	b)	19.9	—	1.1	–0.2	—	—	—	—	—	—	—	20.8	20.8	b)
c) Other deposits	339.7	—	—	—	—	256.4	—	—	—	—	256.4	339.7	596.1	c)	300.6	—	—	—	—	372.0	—	—	—	—	372.0	300.6	672.6	c)
f) Medium- and long-term credits	351.2	—	—	—	—	—	—	—	—	—	351.2	—	351.2	f)	452.0	—	—	—	—	—	—	—	—	—	452.0	—	452.0	f)
g) Bonds	137.4	—	—	53.1	—	143.9	—	—	—	—	334.4	—	334.4	g)	104.7	—	—	151.7	—	–7.6	—	—	—	—	248.8	—	248.8	g)
h) Shares and equity participations	—	—	—	1.5	—	—	—	—	—	—	1.5	—	1.5	h)	—	—	—	0.2	—	—	—	—	—	—	0.2	—	0.2	h)
i) Other financial assets and *liabilities*	6.6	—	—	—	—	—	—	—	—	—	—	6.6	6.6	i)	7.6	—	—	—	—	—	—	—	—	—	—	7.6	7.6	i)
Net financial surplus or *deficit*	60.2	—	2.3	54.6	—	112.5	—	—	—	—	430.7	430.7	=		228.6	—	1.1	152.1	—	379.6	—	—	—	—	329.0	329.0	=	
Social Insurance Funds																												
b) Sight deposits	—	7.6	204.1	—	—	—	—	—	—	—	211.7	—	211.7	b)	—	–6.3	109.7	—	—	—	—	—	—	—	103.4	—	103.4	b)
c) Other deposits	—	—	—	—	—	6.8	—	—	—	—	6.8	—	6.8	c)	—	—	—	—	—	–8.3	—	—	—	—	–8.3	—	–8.3	c)
f) Medium- and long-term credits	32.3	—	—	15.0	—	—	—	—	—	—	47.3	—	47.3	f)	100.6	—	—	2.5	—	—	—	—	—	—	103.1	—	103.1	f)
g) Bonds	8.9	—	—	58.8	—	–5.0	—	—	—	—	62.7	—	62.7	g)	57.3	—	—	173.1	—	–0.7	—	—	—	—	229.7	—	229.7	g)
h) Shares and equity participations	4.9	—	—	—	—	—	—	—	—	—	4.9	—	4.9	h)	..	—	—	—	—	—	—	—	—	—	—	—	—	h)
i) Other financial assets and *liabilities*	173.0	—	—	—	—	1.3	—	—	—	—	1.3	173.0	171.7	i)	206.0	—	—	—	—	–4.6	—	—	—	—	–4.6	206.0	210.6	i)
Net financial surplus or *deficit*	126.9	7.6	204.1	73.8	—	3.1	—	—	—	—	334.7	173.0	161.7		48.1	6.3	109.7	175.6	—	13.6	—	—	—	—	423.3	206.0	217.3	
FOREIGN SECTOR																												
A) Gold	—	62.3	—	—	—	—	—	—	—	—	—	62.3	62.3	A)	—	–147.8	—	—	—	—	—	—	—	—	—	–147.8	–147.8	A)
a) Notes and coin	—	..	1.3	—	—	—	—	—	—	—	—	1.3	1.3	a)	—	..	0.1	—	—	—	—	—	—	—	—	0.1	0.1	a)
b) Sight deposits	—	81.7	275.6	—	—	—	—	—	—	—	357.3	—	357.3	b)	—	–79.6	–184.7	—	—	—	—	—	—	—	–264.3	—	–264.3	b)
Sight deposits	—	—	40.8	—	—	—	—	—	—	—	—	40.8	40.8		—	—	–24.9	—	—	—	—	—	—	—	—	–24.9	–24.9	
c) Other deposits	—	10.4	—	—	—	—	—	—	—	—	10.4	—	10.4	c)	—	–10.4	—	—	—	—	—	—	—	—	–10.4	—	–10.4	c)
Other deposits	—	–4.2	–168.5	—	—	—	—	—	—	—	—	–172.7	–172.7		—	–4.7	124.6	—	—	—	—	—	—	—	—	119.9	119.9	
d) Short-term securities	—	–336.8	—	—	—	—	—	—	—	—	—	–336.8	–336.8	d)	—	480.8	—	—	—	—	—	—	—	—	—	480.8	480.8	d)
e) Short-term credits	—	—	25.5	—	—	—	—	—	—	—	25.5	—	25.5	e)	—	—	5.0	—	—	—	—	—	—	—	5.0	—	5.0	e)
Short-term credits	—	–12.2	18.0	—	—	—	—	—	—	—	—	5.8	5.8		—	–67.2	4.8	—	—	—	—	—	—	—	—	–62.4	–62.4	
f) Medium- and long-term credits	173.6	0.8	—	38.5	—	—	—	—	—	—	212.9	—	212.9	f)	256.4	–0.6	—	126.1	—	—	—	—	—	—	381.9	—	381.9	f)
Medium- and long-term credits	14.4	–6.0	—	26.0	—	—	—	—	—	—	—	34.4	34.4		30.9	–13.9	—	4.5	—	—	—	—	—	—	—	21.5	21.5	
g) Bonds	2.9	—	—	—	—	—	—	—	—	—	2.9	—	2.9	g)	5.9	—	—	—	—	—	—	—	—	—	5.9	—	5.9	g)
Bonds	11.0	15.3	—	—	—	—	—	—	—	—	—	26.3	26.3		—	–130.3	—	—	—	—	—	—	—	—	—	–130.3	–130.3	
h) Shares and equity participations	569.6	—	—	—	—	—	—	—	—	—	569.6	—	569.6	h)	309.9	—	—	—	—	—	—	—	—	—	309.9	—	309.9	h)
Shares and equity participations	34.7	—	—	—	12.9	—	—	—	—	—	—	47.6	47.6		36.2	—	—	—	13.9	—	—	—	—	—	—	50.1	50.1	
i) Other financial assets	—	—	–3.4	—	6.5	—	—	—	—	—	3.1	—	3.1	i)	—	—	7.9	—	6.6	—	—	—	—	—	14.5	—	14.5	i)
Other financial liabilities	913.8	—	—	—	—	—	—	—	—	3.0	—	916.8	916.8		343.3	—	—	—	—	—	—	—	—	2.0	—	345.3	345.3	
Net financial surplus or *deficit*	227.8	374.5	406.1	12.5	6.4	—	—	—	—	3.0	1,181.7	625.8	555.9		161.8	207.5	276.4	121.6	7.3	—	—	—	—	2.0	442.5	652.3	209.8	

IX. *Excerpts from the Governor's Concluding Remarks*

Gentlemen,

This is the fifth time that I am called by my office to report to you on our country's monetary situation. Every year, I have had to give you a picture of quite different economic developments, and over the whole of the five years the chain of events moved from a situation of high promise—with expanding production, stable prices and an external surplus—first to a balance-of-payments crisis and then to stagnation at home. Now I can report on signs of recovery which justify the hope that we may in the near future assemble once more the positive elements of the initial situation and move along the path of growth again, less fast perhaps, but in a more orderly manner.

To do this, we must put to good use the lessons we have learnt, and suffered, in the vicissitudes of recent years. This is why I, who has had to live through them in a position of heavy responsibility, would like to take this opportunity to go beyond the events of the last year alone and to discuss the whole nexus of cause and effect, of action and reaction, which generated the ebb and tide of economic events during the whole five-year cycle.

The means by which public opinion is informed have become more numerous and better. But it is also true that the public at large has become much more interested in economic problems, just because recent changes in business conditions have been so dramatic, because they have so patently affected the situation of individuals and the economic branches in which they work, because government has intervened on such a large scale and because the outlook for the future has been so uncertain. Production, investment, consumption, costs, prices, profits, balance of payments and the relationships between all these magnitudes have ceased to be esoteric logical categories intelligible only to a small circle of experts, and have become the subjects of discussion in which political parties, trade unions and Parliament join with increasing frequency. This is a sign that we are progressing towards a more truly democratic order in which the members of the national community take conscious responsibility for the affairs of their country.

The complex events of the last few years, our successes and our failures, gain added interest, from the point of view both of economic policy and of economic analysis, by the great variety of new and unexpected factors. It has become clear, first of all, to what a large extent the development of a modern economy is governed by forces which cannot easily be controlled by the monetary authorities. Later, in the phase of adjustment, the Italian economy was seen to have retained its full capacity to transfer resources from domestic to external uses through equilibrating processes of a monetary nature which neither interrupted, let alone reversed, our country's progress toward integration with the world market.

While I shall limit my remarks to the sphere of competence of a central bank, I yet hope to make a contribution to the knowledge and understanding of all these matters by discussing in depth those aspects of monetary policy which are our more immediate responsibility. If I give no more than brief mention to strictly cyclical aspects having to do with production, prices and the balance of payments, it is in part because, as I have said, these are discussed frequently and widely, if only because people are anxious to discover in them at once any hopeful signs that may appear. In any event, these are thoroughly examined in the separate chapters of this Report.

The International Monetary System and Italy's Return to External Balance.— Before turning to the problems of the Italian economy itself, however, I feel I should first call your attention to a set of wider problems which have been the subject of so many new proposals and such lively debate recently, even if I cannot in my brief remarks do adequate justice to the complexity of the argument. I have in mind the problems of the present and future of the international monetary system.

Such as it is today, this system makes it possible to raise with lightning speed the financial resources needed to break any speculative attack launched upon the currency of a country while it takes steps to re-equilibrate its balance of payments. This has been demonstrated quite recently when sterling came under heavy pressure and the United Kingdom received financial assistance on an unprecedented scale, first through central bank support and subsequently through drawing on the ordinary resources of the International Monetary Fund as well as on special resources which the latter raised under the General Arrangements to Borrow.

But to acknowledge these merits of the system does not absolve us from the obligation to look also for any demerits it may have and for ways of eliminating them.

The most serious drawback of the current international monetary system is commonly stated to be that the chief source of international liquidity creation is the deficit in the United States balance of payments. Since 1958, the United States incurred a total deficit of 21 billion dollars, and only 7 billion of it were covered by gold sales from the U.S. Treasury to the central banks of surplus countries, especially in continental Europe. The remaining 14 billion dollars largely accumulated in commercial and central banks elsewhere than in the United States, and more than one third of them, again, in continental Europe. To the extent that they are in central banks, they are used as currency reserves.

The critics of the present system say that in the absence of these dollar balances the government of the United States would have been forced to re-establish external equilibrium quickly. They also say that the very size of the U.S. deficit and the fact that it was partly financed by European central banks purchasing dollars against national currencies were one of the causes, and perhaps the chief cause, of the inflationary pressures in Europe. The argument is that prices are pushed up by the excessive purchasing power injected into the market by the dollar purchases of the central banks, and that higher prices in turn push up wages. It is also argued that simply to aim at aligning wage increases with productivity increases without doing anything about this excess flow of monetary means to the market would mean wanting to remove the effects without eliminating the cause.

The conclusion of all this is that the only dam which can hold back the flood of purchasing power which originates in the United States and threatens to submerge Europe is a return to the gold standard.

There was a time when ideas of this kind had a consistent counterpart in the view that the mechanism of competition could, and should be left to, re-establish external balance through appropriate wage adjustments.

In the more recent pronouncements on the gold standard this link with other, parallel, processes of spontaneous adjustment has been passed over in silence. Most likely, it was not thought possible to resuscitate a model of the labour market which has been overtaken by modern conditions. Today, the institutional presence of trade unions has become so decisive that it has been said of them that their conduct is ultimately the arbiter of monetary stability. But we may well ask whether the gold standard, so stripped of the other elements which formed part of the system, can be revived at all, and if so, whether it should be revived if it means not indeed a return to competitive labour markets but adaptation at the cost of intolerable levels of unemployment.

Because such repercussions are possible, I have my doubts about the wisdom of an outright return to the gold standard. I would add that while I regard the joint responsibility for monetary stability which theory attributes to the trade unions as a matter of highly desirable progress and maturity, I do not believe that the monetary authorities may neglect to put such means as they possess to resolute use whenever circumstances require, so as to safeguard confidence in the currency.

Others propose that we should abandon the fixed exchange rates which underlie our present international monetary system and should adopt instead a system of flexible exchange rates. This proposal is placed in a different context, but still has a certain kinship with the model of freely operating market forces. But it must be remembered that flexible exchange rates are only apparently an expression of market forces. In practice, government and monetary authorities can and do influence both the spot and the forward rate and they can and do control short-term capital movements, so that flexible exchange rates would be a solution strongly subject to economic policy purposes which may conflict with the orderly expansion of world trade and imply the risk that one country may shift its own difficulties onto other countries. What would happen in fact is that we would do away with something which today is a firm point in our economic system and replace it with a mobile barrier which could hardly be protected from the pressure of particular interests.

In actual fact, the gold standard as such, that is, to the extent that it worked according to its own logic and was not arbitrarily amended by correctives superimposed upon its purely automatic mechanism, presupposed an economic setting in which the size of the public sector, the degree of sectional organization of economic forces and technological rigidities were very different indeed from those we know today. Just to stress a few rules of monetary conduct without reference to the underlying structural conditions which also were an integral part of the system, contributes nothing to an understanding of the problems either of the past or of the present. As has been made abundantly clear by many and well-documented studies, much was done even in the past by the deliberate intervention of monetary authorities, by the use of various techniques of intervention and by ad-hoc forms of reciprocal assistance, to reconcile the internal requirements of monetary policy more flexibly with those deriving from the intrinsically international nature of the gold standard.

However, a critical re-appraisal of the past in no way invalidates the principle that no country can go on for long either accumulating or losing reserves and that situations of this kind demand appropriate corrective policies. But to recognize this fundamental need does not mean, or imply, that whatever adaptations are necessary should no longer be made with deliberate judgement, at a measured pace and with the help of institutional collaboration. All this has become part and parcel of our international monetary system today, and there can be no question of renouncing it. The same reasons lead me to say once more, as I have often done before, that I take a very favourable view of the various forms which monetary co-operation between governments and central banks has taken in the last few years and also quite recently. This co-operation constitutes not a haphazard and occasional sort of support which would almost be a symptom of the present system's weakness, but on the contrary links the working of the system to responsible human decisions and so testifies to its flexibility and development potential.

Whatever form this co-operation has taken on the multilateral and on the bilateral plane, Italy has always gone along with it in the firm conviction that this road was patently preferable to any alternative open to us at the moment, such as devaluation by countries whose currencies are under pressure or else the adoption of flexible exchange rates. The effects of these alternatives can, of course, be assessed only by conjecture and hypothesis, and therefore they leave a wide margin of uncertainty as to what repercussions and, most likely, chain of emulation would actually follow. Reciprocal aid, on the other hand, is at one and the same time the fruit of operational practices which have stood the test of experience and a means of evaluating the procedures adopted and improving them in the light of experience.

It is indeed precisely thanks to this practical and empirical approach that as a matter of monetary techniques a credit component has definitely come to stay as part of external liquidity in our international monetary system, in whatever way we may amend it. But claims rest on trust, and because of that require that the authorities which hold reserves should be free to choose by what reserve assets they wish to supplement gold. I say this with respect to the currencies which exercised reserve functions in the past and still do: the dollar, sterling and French franc. These currencies have become widely acceptable through a process of free conditioning and in substance because they are directly or indirectly convertible into gold and, ultimately, into goods and services. If, on the other hand, new reserve assets are created on the basis of world trade needs by formal decision either within the International Monetary Fund, or more suitably, within the Group of Ten in association with the Fund, then the acceptability of these reserve assets would have to be governed by agreements which lay down the obligations of creditors and debtors alike.

For these reasons, I believe that the timely studies which were made last year on the functioning of the international monetary system and its probable future needs of liquidity should be carried forward in the same spirit of constructive collaboration which suggested this method in the first place. The purpose should be not to remove the problems under investigation from public discussion, but to look for the basis of possible solutions without indulging in utopian expectations or oversimplifying predilections which seem hardly compatible with the complex working of modern economies.

Italy's support of this approach has, among other things, found expression in the choice of one of our countrymen to become chairman of the Study Group which has been asked to evaluate the various proposals for the creation of new reserve assets to supplement gold, as and when assessed long-term needs so require.

Another proposal which has come up in the course of reappraising the working of the international monetary system is that there should be multilateral surveillance of the ways and means of financing balance-of-payments disequilibria.

I believe that procedures of this kind may prove useful in adapting the volume and forms of finance to the nature of the imbalance; once we have more knowledge of these questions, as we should soon have thanks to the studies in hand, they are also likely to lead to the speedy adoption of such corrective measures as may be found expedient in any particular case.

There are, definitely, ways in which our present international monetary system can evolve, and, as I have said, they imply the continued use of fiduciary assets to supplement gold in reserves. However, the extent of this fiduciary component should not be tied to the balance-of-payments vicissitudes of particular countries, but should be ruled by world trade needs and its creation subject to multilateral surveillance. Within the same framework, we might also work towards agreements on the proportions to be observed in the qualitative composition of reserves as between traditional assets and such new ones as may come to join them.

A common policy of exchange reserve administration could combine different objectives, as follows:

(a) An undertaking by central banks to finance balance-of-payments surpluses and deficits subject to an agreed proportion of gold and dollars or other reserve currencies would remove the process of creating fiduciary international liquidity assets from the discretion of countries which issue reserve currencies.

(b) At the same time, changes in the proportion of gold and other reserve assets would enable the volume of the credit element to be adapted from time to time to international liquidity needs, without tying its creation to the supply of newly mined gold.

From the point of view of their effects on the volume of international liquidity, these solutions are equivalent to a change in the price of gold; but unlike the latter, which would have patently undesirable consequences, they would make room for flexible adjustments in the light of changing conditions on the world market. I would say that these solutions appear to me as an indispensable condition of any progress toward closer monetary integration among the industrial countries and also of any possible reform of the international monetary system. No reform should overlook the need for a mechanism which can, if it proves necessary, provide the world economy with additional owned reserves and possibly with automatic credits. Nor should reform try to do away with reserve currencies, but should instead take care to safeguard equal treatment for all the currencies of major industrial countries. No reform, finally, should refuse to acknowledge that the sterling balances of the United Kingdom are, at least to some extent, a common problem of us all. If these conditions are fulfilled, the controversy regarding the nature of new reserve assets and the method of their creation and distribution should surely be amenable to reconciliation.

Lastly, wider recourse to the International Monetary Fund would have the distinct advantage of channelling to the Fund part of those central-bank debts and credits which are components of international liquidity. This would mean that credits to finance external imbalances would remain within the limits of each country's quota with the International Monetary Fund.

Turning now more particularly to the problems of the Italian economy, I shall focus my remarks on what I consider to be the two main responsibilities of monetary policy, namely, to maintain equilibrium in external payments, and to encourage the formation of saving and control the flow of credit towards investment.

In discharging our responsibility with respect to external equilibrium, we availed ourselves of the manoeuvering space which our currency reserves and international monetary collaboration allowed us, but we accepted the condition of a stable rate of exchange. This very condition implies for our second main responsibility that we must determine the volume and guide the flow of credit in such a way as to maintain a certain degree of domestic price stability.

The transition of Italy's balance of payments from a period of deficit into one of surplus was due in large extent to the combined effect of the economic system's own forces and our policy of containing credit expansion. The Italian economy was protected by deep ranks of firms which had previously raised their efficiency by investment, and this is why foreign demand could expand at a time of falling domestic demand. We only need to look at the output and export figures of the various branches of industry, and at those of domestic supply and imports to see what conspicuous proportions the substitution of foreign for domestic demand and of domestic for foreign supply assumed in the most dynamic sectors of our economy —and these are the self-same sectors which enlarged and modernized their productive capacity thanks to the credit expansion of 1962 and 1963.

But the monetary authorities eventually had to take steps to hold back credit expansion gradually, if only to prevent an excess of domestic money supply from propagating inflationary effects abroad through persistent deficits in the balance of payments. It is not proper for a responsible member of the international community to go on accumulating deficits of the order of magnitude as occurred between the fourth quarter of 1962 and the first quarter of 1964; even when their effects are mitigated, as they were in our case, by international credits, they demand forceful countermeasures. During that period, we incurred a total deficit of 1,855 million dollars, and we financed it by mobilizing one after the other our sources of external liquidity. The lion's share of 955 million dollars was drawn from the short-term credits which Italian banks obtained from foreign banks; we liquidated 115 million dollars' worth of short- and medium-term assets; we incurred 110 million dollars of short-term liabilities; we used up 375 million dollars of convertible currencies and drew another 202 million of them from the International Monetary Fund; only the small residual amount was covered by gold sales.

This is how we surrounded our gold reserves by a protective layer which absorbed the great bulk of the deficit. The effects are now manifest in the net foreign debts of our banking system. In due time we shall redeem these debts, but it is not least for this reason that I believe that policy decisions regarding the use of reserves should be based on the proportion of gold not in gross, but in net reserves.

I have heard it said that the measures taken in Italy to get external payments back into balance were too harsh, that the crisis was not as severe as the monetary authorities thought and could have been met with milder action. But a deficit of 1,855 million dollars in 18 months is certainly not small by international standards. The persistence of deficits of similar magnitude in the balance of payments of the United States has indeed caused some voices to be raised in favour of measures resting on the principle that no nation should be allowed to export its own inflation through its balance-of-payments deficit, and that any deficit country should settle in gold and only in gold, restricting its money supply to match the loss of gold reserves. It makes one shudder to think what the consequences would have been in Italy, where the economy experienced a credit tightness judged to be excessively severe, even though the monetary authorities made good, and more than good, the whole of the liquidity drain of the external deficit. The plain figures bear witness to the gravity of the crisis which our country suffered and by that very fact show up the extent of the effort by which our economy overcame this crisis. Notwithstanding the sacrifice it involved for our level of investment, we can appreciate the full measure of this effort by recalling that virtually all the additional real resources produced in the country in 1964 were used to improve the balance of our exchange of goods and services with abroad.

During the twelve months ending in March of this year we had a surplus of 1,282 million dollars in our balance of payments. Of this amount, 297 million went to reducing the banks' net indebtedness abroad. We added 736 million dollars to our gold and convertible currency reserves and built up a credit position of 173 million with the International Monetary Fund; the rest was used up in minor assets.

Last April we transferred to the accounts of the Italian Exchange Office gold assets previously credited to banks and bought some gold from the U.S. Treasury. In this way we raised our gold holdings back to what they were on 28 February 1964, just ahead of that fateful month in which the balance-of payments crisis exploded in our faces. The wounds which external deficits succeeding each other throughout 18 months inflicted upon our gold reserves have healed.

I would not wish to state this fact without adding once more a tribute to the monetary authorities in other countries, for their prompt and generous help in the hour of our greatest need. I also want to say how much we appreciate the proofs of confidence shown to us by the long-term lenders among the international agencies, such as the International Bank for Reconstruction and Development, which recently extended another 100 million dollar loan to the Cassa per il Mezzogiorno, or the European Investment Bank, which by now has a total 341 million dollars outstanding in loans to Italy.

The Control of Bank Liquidity. The Use of Credit by Firms in the Public and the Private Sector.— As regards the problems of monetary control I want to take issue first with the widespread view that a period of expanding production was followed by a period of contraction because of credit restrictions introduced by the decision of the monetary authorities. We are here in the realm of statistically verifiable facts, and can reply by quoting figures about the events under discussion.

Our budgetary and monetary policy were repeatedly criticized in international circles as being altogether too rash. Not longer ago than May 1964 some of this international advice was still that we should not only contain the growth of public expenditure within the limits of foreseeable real income growth, but also space out our investment expenditure more gradually over time, stiffen our income tax and perhaps even raise at once our turnover tax rate. The idea was that an increase in revenue of some 400-500 billion lire during the financial year should be used to reduce the budget deficit, and that we should re-inforce the policy of credit containment, which we initiated in the course of 1963, by imposing a strict ceiling on credit expansion.

The Italian government was not in full agreement with this diagnosis nor, therefore, with the therapy proposed. The government did not then, nor did it on earlier occasions, introduce measures to restrict total demand, with the exception of some hire-purchase sales. What the government did instead was to take steps intended to re-shape the structure of demand, by channelling the purchasing power withdrawn from consumption towards the financing of public and private investment.

Public spending, understood as the sum of expenditure by government, autonomous government agencies and local authorities, did not at any moment exercise deflationary effects, as some say; and this is true whether we look at public expenditure from the point of view of its volume, the way in which it was financed or its purposes. On the contrary, the effect was inflationary: public expenditure has been growing uninterruptedly, mainly under the impact of direct or indirect rises in personnel costs, which meant that no major new flows of real resources were generated. This was another reason for the inflationary effects, for to the extent that growing expenditure was covered by taxation, it helped to push up costs, and to the extent that it was financed by borrowing, it raised the supply of money, quasi-money and securities. The new debts contracted in 1964 by government, autonomous government agencies and local authorities between them absorbed one third of all the savings which the nation, including the Social Insurance Funds, set aside during the same year in cash, deposited with the credit system or invested in securities.

When I spoke to you three years ago at our General Meeting of Shareholders, I drew your attention to the circumstance that in our economy labour costs were racing ahead of productivity, and I pointed out that to the extent that higher labour costs were not transferred onto prices, firms saw their self-financing capacity impaired and ultimately had to rely more heavily on outside sources of finance. While all this was happening, I added, the public sector's investment programmes in excess of its possible saving were tending to expand, so that public investment also was becoming more dependent upon borrowing. These public claims, too, largely concentrate on the special credit institutes, which in their turn raise the bulk of their loanable funds by bond issues.

In view of this situation and of the foreseeable need for funds in connection with the transfer of electricity companies to E.N.E.L., the new National Electricity Board, I announced that we would take steps to widen the capital market; the central bank, I said, would help to give the economy a system in which funds can easily be transferred from one category of uses to another and channelled towards those which are held to be most in the public interest. The intention was to improve the links which connect the money market with the capital market and make the interest rates in both more closely interdependent. But I also warned that the flow of finance would still have to be conditioned by the real factors underlying the ultimate sources of the supply of saving.

Credits advanced on the short, medium and long term to the private and public sectors of the economy, excluding the Treasury, increased uninterruptedly throughout the years 1961 to 1963. The figures are 3,334, 4,325 and 4,527 billion lire. Last year long-term credits to the economy still expanded, but short-term credits to it dropped sharply in spite of greater bank liquidity.

Now, the size of the capital market is measured by the sum of long-term funds, including the proceeds of equity issues by companies, which reach the economy in any given period. The figures show strong expansion between 1961 and 1962, then slight contraction in 1963, followed by renewed growth to a record 2,844 billion lire in 1964.

The capital market was widened by transferring monetary assets to it through two main channels, as follows:

(a) Bond purchases by the Bank of Italy and other institutions which obtain from it the liquid funds which they invest; bond purchases by banks, financed by their own means and by the sale of Treasury Bills to the Bank of Italy on the occasion of the change in the composition of compulsory bank reserves. All told, the credit system took up bonds in the value of 663 billion lire in 1963 and of 845 billion in 1964.

(b) Net loans by banks to their Special Sections handling long-term credit and to special credit institutes in which they own part of the equity; direct loans especially by savings banks and their banking association, and by the Central Post Office Savings Fund. The total funds involved in operations of this kind amounted to 575 billion lire in 1963 and to 767 billion in 1964.

Bank liquidity depends in some part upon interventions by the monetary authorities, which interventions in turn may have an immediate or a delayed effect; in some part it depends upon other, autonomous, factors. Accordingly, three liquidity effects have been quantified separately in this Report [Table 34], as deriving from autonomous factors or intervention by monetary authorities, and in the latter case, from their own operations or from operations they authorize.

Let us again look at the figures, taking the two nine-month periods from April to December 1962 and 1963, which are usually described as periods of abundant and tight credit, respectively. The increase in bank liquidity imputable to direct operations by the monetary authorities was 367 billion lire in the first case, and 737 billion in the second. In other words, direct operations by the monetary authorities created twice as much new liquid assets in the period of allegedly tight credit than they did in that of allegedly abundant credit. During the nine months of alleged credit shortage, the authorities thus more than made good the liquidity loss due to the balance-of-payment deficit, and in addition left the banks free to raise another 268 billion lire of liquid assets by borrowing more abroad.

There are yet other figures by which to prove my point. Let us look at the total money supply injected into the economy through credits and security purchases by the banking system as a whole, including the Central Post Office Savings Fund; we see that during the period when it was our policy to contain the credit expansion, more credit was actually created than during the corresponding period of the preceding year. The figure for April-December 1963 was 2,736 billion lire, as against 2,433 billion for April-December 1962. Credits to the Treasury net of the latter's credits to the Economy amounted to 154 and 190 billion lire, respectively, during the last three quarters of 1963 and 1962, and the combined figures for the two sectors were 2,890 billion lire in 1963 and 2,623 billion in 1962—always taking only the last nine months of the year [Table 35].

During the period April-December 1963 some 614 billion lire of the money assets which the banks lent to the Economy and the Treasury were spent on financing the external deficit, which was largely due to excess imports of goods and services. To this extent the funds did not return to the banking system, and consequently the credit expansion of 2,890 billion lire increased the public's liquid assets, including primary and secondary liquidities, by only 2,276 billion.

At the same time the index of industrial production showed that the process of expansion was coming to a halt. What happened was that even a credit expansion of such exceptional magnitude as occurred throughout the second half of 1963 was unable to offset the capital shortage from which firms suffered as a result of cost increases not passed on to prices. The consequent contraction of investment set in motion a process of recession; credit expansion did mitigate its severity, but went beyond the public's willingness to hold liquid assets.

Monetary policy during the period April to December 1964 was designed to let bank liquidity rise under the impact of an excess of foreign-exchange purchases over foreign-exchange sales in connection with the balance-of-payments surplus, and indeed to create yet additional liquidity by other operations. As a result, the banking system acquired twice as much liquid assets as it had done during the corresponding period of 1963, but this liquidity gain failed to have any multiplying effect on credit creation. During these nine months of 1964 credit, including security purchases, expanded by 1,626 billion lire and the public's gross liquid assets by 2,383 billion, the difference being equal to the surplus in the balance of payments.

Its larger supply of liquid funds induced the banking system to extend more credit especially for public works and land reclamation, and to firms in the mineral oils, chemical, metallurgical and engineering industries; but firms did not feel induced to use these credits in correspondingly higher measure. The economic system seemed to be stunned by the succession of events to which I drew your attention more particularly on the occasion of our Meeting on 31 May 1963; the prevailing climate of uncertainty was as yet hardly relieved by the recent introduction of counter-cyclical measures.

Now let us draw some conclusions:

(a) The statistics do not bear out the statement that a period of exceptional credit expansion was followed by one of exceptional contraction. Intervention by the monetary authorities occasioned more liquidity creation during the period of alleged credit shortage than during that of alleged abundance.

(b) Long-term credit flows to the economy expanded strongly in 1962, remained at high levels in 1963 and again expanded in 1964. Short-term credit expanded as much in the second half of 1963 as it had done in 1962, and when it stopped expanding in 1964, it was at a time of greatly increased bank liquidity.

(c) In the presence of yawning balance-of-payments deficits, credit supply was kept below demand for credit and thereby the formation of additional monetary assets was gradually brought closer to the public's willingness to hold them, and so we created the conditions which enabled the external deficit eventually to be eliminated.

Everything I have said so far, and the above conclusions, rest on an analysis of aggregate magnitudes. If we examine the underlying separate figures, we see disparities of sometimes major extent in the behaviour of big and small banks, big and small firms, and firms in the public and the private sector of the economy.

When the banks were suddenly faced with an increase both in the demand for new credit and in the utilization of existing credit lines, they reacted by keeping a closer watch on the amount of each advance. Some firm or other may have found itself able to borrow less as a result, though the sum of credits actually drawn increased as I have said.

The behaviour of the banking system has come in for some criticism. It has been said that the banks restricted credit just at the moment when firms badly needed more loans. But it must not be forgotten that when the credits were originally conceded, the requirements of each borrower had been assessed by the yardstick of normal conditions, conditions, that is, when credit requirements tend to vary within limits more or less predictable on the basis of experience, and moreover to vary in opposite directions as between different sectors and firms. But now firms were suddenly deprived of a large part of the funds with which they formerly used to finance production, and so they all rushed to the banks with insistent requests for new credits and wanting to draw more on their existing credit lines even than had originally been arranged. It was the banks which ultimately had to sustain the shock of the vast changes in income distribution which had come about in so short a time to the accompaniment of a sharp rise in prices, and this is why the flood of credit demand converging upon the banks had to be dammed in.

There is a lesson to be learnt from these events, and it is this. If the distribution of income among the factors of production had the benefit of the responsible collaboration of organized groups, we would be creating one of the conditions necessary not only for safeguarding the purchasing power of money, but also for a credit supply not subject to wild fluctuations.

This latter purpose will be well served by the activities of the Central Risk Pool and by careful interpretation of the information it furnishes. The limit above which individual credits have to be notified has now been lowered to 100 million lire and we expect to lower it again. I think I can say that we have set up a service organized on modern lines and employing the most advanced techniques.

The differences in bank reactions to large, medium-sized and small firms are at least in part attributable to the different degrees of credit utilization by these three categories. A survey of data come to hand at the Central Risk Pool between March 1964 and March 1965 showed that firms to which total credits between 250 million and 1 billion lire had been extended actually drew the largest proportion of these credits; above the 1-billion line, credit utilization was generally somewhat lower and, after September 1964, decreased more rapidly than the average, and this was especially marked in the highest size class of total credit extended. As regards smaller firms, which had borrowed a total of less than 250 million lire each, the latest investigations seem to suggest that these are in the habit, perhaps not least for prestige reasons, to take up more credit than they normally need; this gives them a more flexible and cheaper margin of cash than other firms dispose of.

If the credit distribution is such that firms in the medium range of total borrowing use the greatest proportion of the credits extended to them, these same firms naturally suffer most at a time when an effort is made to contain the credit expansion.

I have more than once had occasion to draw attention to the element of rigidity deriving from the circumstance that many large firms had in hand major investment programmes for plant extension and new construction, just when the cost/benefit ratio changed to their detriment and deprived them of some of the funds on which they had counted. Because the construction programmes which were already going forward could not be interrupted without destruction of wealth, the large firms needed more long-term and short-term credit, and as access to the capital market became harder, they had to rely more on short-term credit. Thus they drew heavily on such credit facilities as they had left unused so far, and more especially on overdrafts on current accounts; the medium-sized firms, on the other hand, which had already used up more of their credit facilities, soon came up against an absolute barrier.

The increased pressure of the large firms' demand for bank credit concentrated largely on the biggest banks, and it was the latter which had to rely most on recourse to the Bank of Italy and on borrowing abroad. Once current investment programmes were completed, the credit demand of the large firms, which had not in the meantime started new programmes of similar magnitude and also found the capital market more receptive, became less pressing, with a consequent easing of the strain for the banks upon which this demand had largely converged. But the first to respond to the signs of recovery in production were the medium-sized banks; their ready reduction of the interest charged on loans proved an incentive for the larger banks to do likewise.

We made all these adjustments in the money supply without altering Bank Rate, contrary to some of the advice proffered to us at international level. In last year's Annual Report we underlined the consequences of a system under which banks raise funds from the Bank of Italy, from other Italian banks and from foreign banks at different rates of interest. It may be worth probing a little more deeply into this matter and trying to identify the elements of rigidity and flexibility in our pattern of interest rates.

It is not news to anyone that we have often had occasion to point out that the system of interest rates the banks apply in their relations with clients is far from perfect and that something would have to be done about it one day. Under this system there is a lower limit for interest charged to clients, and a ceiling for interest paid on deposits. It follows that at a time when money is scarce and the rates charged to clients go up, the banks, if they stick to the rules, should raise the interest on deposits to its ceiling, but not beyond. Conversely, when loanable funds are in ample supply and the banks charge less for loans, they can never charge less than the lower limit. This lower limit is connected with the level of Bank Rate, and would go down if the latter were lowered. But the same result could be obtained without any change in Bank Rate, simply by altering the relationship between the rediscount rate and the interest rates applicable to the various lending operations.

During the 18 months when our balance of payments was in the red, the money supply generated by the budget deficit offset that absorbed by the external deficit; operations carried out, or permitted, by the monetary authorities created an additional 1,597 billion lire of liquid assets, of which 404 came from the Bank of Italy through rediscounts, 473 were borrowed from banks abroad, and the rest was mobilized mainly through security operations and changes in the rules concerning compulsory reserves. The rate of interest paid for foreign bank credits was higher than Bank Rate. Yet the very volume of these credits demonstrates that high interest rates are no deterrent to large-scale borrowing by the banks when they need funds.

The system of interest rates paid and charged by banks under the interbank agreement certainly does contain an element of artificiality, in that it prevents the rates from adapting themselves flexibly to the conditions of supply and demand with respect to money resources. This artificiality will have to be removed sooner or later. But, it should be added, if we want a more competitive banking system, we shall need gradually to reorganize it. In some cases this means merging separate banks, and this we are doing, with due caution and with the collaboration of the banking associations; however, this implies no departure from the objective of having our credit system based on a large number of mutually independent decision centres. Through its Inspection Service, which was very active last year, the Bank of Italy learns of unsound positions and in such cases promotes a concentration of banks which is better in line with the size of a market open to domestic and international competition.

The slowing-down of the Italian economy in 1963 and 1964 could hardly fail to freeze up some funds and occasion some losses. Neither phenomenon assumed the sort of proportions known from earlier recessions, but the banks did feel the shock, not least because of the very size of their commitments in firms, and especially those of more recent creation. The banking system as a whole stood up well enough, thanks to the safeguards by which the Bank Law of 1936 protects the public's savings. There were some victims, but they were usually small banks and more especially banks whose majority shareholders had channelled credit to other firms they owned and whose management, for one reason or another, proved ill chosen.

Wherever a critical position developed, we intervened in compliance with what we believe to be the fundamental principle of the 1936 Law, namely the protection of depositors. The willing collaboration of banks and banking associations greatly facilitated our task. In some cases we took steps to have shareholders replaced. I would note in passing that the absence of any rules which make the transfer of equity in corporate banks subject to control hinders us in our supervisory functions. We can strengthen the Service; we can multiply inspections. But we cannot close our eyes to the fact that, however many inspections we do carry out, we cannot safeguard depositors unless the bank managers to whose astute judgement the public entrusts its savings, conduct themselves, as in fact they do, with the strictest correctness.

The laws which govern savings banks and stress the public-interest aspect of savings deposits, and the Bank Law of 1936 which reaffirmed the same principle, were both intended to make sure that no person unfit for the heavy responsibility of looking after other people's wealth had access to the board of directors or the management of any bank. I think it is necessary to recall these principles of the law. I think also that it is my duty to point out what serious consequences would follow if the spirit of the law failed to be observed both by the public sector which is responsible for nominating the managing staff of savings banks, public-law credit institutes and the banks of national interest, and by all those with administrative responsibilities in people's co-operative banks, other credit co-operatives or private banking firms.

It is incumbent upon those who fashion credit policy to adjust it continually to the needs of a growing economy, and more especially to do everything they can to eliminate the obstacles which impede the entry of new firms and which are enhanced by the very discontinuities created by technological progress. In many sectors the optimum size a firm must have to be competitive tends to grow, so much so that in some cases it might become necessary to reorganize the whole set of firms belonging to any sector with a view to adapting company structure to the new technical conditions. A case in point is the cotton industry, which in other market economies has been reorganized systematically by measures jointly planned by the public authorities and the firms themselves. All this, for the rest, is by no means extraneous to the institutional set-up of the credit system, which also needs to modernize itself with a view to making a positive contribution to the maintenance of effective competition.

One of the causes of an investment distribution other than optimal from the point of view of the system as a whole is the influence which the financial power of firms has on investment decisions. In so far as they have new techniques or new products to introduce, the big concerns can more easily raise the funds they need. The danger is enhanced when these concerns can command preferential treatment because they belong to the public sector.

Large firms, especially in the public sector, have the advantage over small ones that they can borrow at the same time from several banks. The statistics confirm that the number of banks which lend to any one client is highest when the total credit is largest, and lowest when the total credit is smallest.

Credits of small and medium amount are those scrutinized most closely. Banks seem to think that such credits involve heavier risks because the firms to which they are extended might go bankrupt, whereas credits to large firms, especially those in the public sector, are thought to be immune from this particular risk.

In all cases when several banks extend credit to one and the same firm, the group of lenders includes big banks and small banks. The big banks are surrounded by a cluster of small ones, as if the formers' judgement in itself were a sufficient guarantee; it looks occasionally as if the smaller banks proportioned their lending to that of the big ones, simply applying a reduction factor.

So much about the rigidities which prevent the volume of credits adjusting itself to changing business conditions and which tend to throw the main burden of such adjustment onto the small and medium-sized firms of the private sector. The principal reasons for these rigidities are the large requirements of the public sector and especially local authorities, as well as those for major public works and large-scale industrial plant, constructed on behalf of firms in both the private and public sector, under programmes stretching over several years. Another source of rigidity is the pressure which such firms exercise on short-term credit whenever they finance their requirements (as in fact they do) by recourse to short-term or indeed to long-term credit just at a time when medium-sized firms should have more short-term credit.

In modern economies investment in public works and industrial plant under programmes spaced out over a number of years tends to absorb a growing share of total investment. But this requires a continuous flow of saving, because otherwise it might become necessary to finance the completion of the programmes by expanding liquidity. Financially advanced countries can count on a continuous flow of saving because of the sheer volume of insurance, life and pension funds. In our country the creation of an efficient capital market is impeded by the scarcity of pension schemes based on accumulated funds and by the proposal that they should be abandoned altogether.

The Economie Factors behind the Monetary Factors and their Interdependence.— Having assessed the measure of the monetary phenomena which accompanied our economy through its vicissitudes during the last few years, and the part attributable to public expenditure, external relations and the credit system, we should now try to analyse what was behind these monetary phenomena. To this end we need to look further into the past and recall certain features of the development process which followed postwar reconstruction from, say, 1950 onward. Starting from a position of pronounced and almost universal technical backwardness, the Italian economy has moved forward since that time to levels where some industries at least can stand comparison with those of the most advanced economies. Over the course of those years, new doses of factors of production called forth more than proportional increases in output. Assuming that these increases, to the extent that they were more than proportional to the additional capital and labour employed, were attributable to technical innovation, statistics show the latter to have been responsible for about half our income growth since 1950.

The largest doses of new capital and labour, and the lion's share of technical innovations, went into industry, and this is where, therefore, the development process concentrated. The supply and income of the industrial sector grew at a strikingly faster rate than aggregate supply and income, and demand for the products of other sectors outpaced their supply. Foreign demand was in continuous expansion and, by creating outlets abroad for Italy's excess supply of industrial goods, played an essential part in sustaining and guiding economic development. The growth of supply in industry was not adequately reflected in a fall of prices for industrial goods, and excess demand in other sectors pushed up the prices of other goods and of services.

As trade with the world at large intensified, domestic prices came more and more under the influence of international prices, and wages, too, rose towards the levels of the industrially most advanced countries. This upward movement gained added impetus from the growing pull exercised upon our labour force by countries which use Italian workers on a large scale and found the inflow of labour from elsewhere interrupted in the middle of a boom.

The tendency of Italian wages to approach levels prevalent in countries with much higher average incomes per person employed aggravated the strains to which the system of production was already subject. If industrial wages were tending towards equality with those paid elsewhere in the European Economic Community, this was bound to widen the gap between labour incomes in different sectors at home. The very widening of the range of wages generated pressure to narrow it down again by raising the lowest wages. Under the cumulative effect of the original impulse and the successive sectoral adjustments, average wages in the system as a whole rose more than productivity; at the same time the growing concentration of labour forces in the large urban conglomerates, which offered better chances of economic advancement, created a climate in which wage claims were pressed home more and more vigorously.

If we look at our situation in comparison with that of the industrial countries with which our relations are closest, we see that for a long time our economy's rate of growth matched or exceeded theirs, then fell behind theirs during the two years 1962 and 1963, until, most recently, economic growth in these countries still continued but ours lost its impetus and almost came to a halt.

Let us look more closely at the period when production developed fastest. In this period, we can identify the following features. Average cost tended to fall, and this was reflected in an increase in exports thanks to more competitive prices; expanding exports drew factors of production into the most competitive sectors; the fall in average cost, which was only partly passed on to prices, raised profits and hence investment in plant, and this in turn further raised the productivity of labour; the more productivity rose, the more our goods became competitive and encountered growing demand; in this way job opportunities went on increasing to the point when labour, and especially skilled labour, began to be scarce. But we note also a signal failure to use income for social investment to create the sort of environment without which the orderly progress of a society based on the respect of human liberty would be very difficult indeed.

In these conditions wages began to rise, and with them average costs. To the extent that these increases were passed on to prices, they lowered our competitive strength and curtailed foreign demand; to the extent that they were not passed on to prices, they cut into profit margins. The result was a smaller propensity to invest, and hence a smaller demand for capital goods and ultimately a smaller total demand.

It would have been possible for the monetary authorities to keep up the volume of investment by expanding money supply to the extent necessary to let firms reconstitute their profit margins. But such a policy could not have gone beyond certain limits. Since we deal with the rest of the world on the basis of a fixed exchange rate, lower exports and higher imports would indeed have held back the price rise, but then our balance of payments would have got deeper and deeper into the red. With costs still going up, the position of firms would have become yet more unbalanced and the success of any policy to boost, or relaunch, investment would have been jeopardized.

To sum up, we can say that any development process deriving from an expansion of foreign demand can continue only so long as the condition upon which it depends continues, that is, so long as average costs do not rise more than abroad. When this condition comes to fail, development slows down. This began to happen in Italy in 1962 and we gave the warning signal in our Annual Report to Shareholders on 30 May of that very year. In addition to the weakening of the pull of foreign demand, investment demand also fell off as self-financing capacity declined under the impact of a cost inflation (wages, social charges, taxes).

The effects of the contraction of investment in industrial plant was aggravated by a fall in housing investment, with the result that the flow of income to these sectors lessened and with it their demand for consumer goods. Thus the impulse was propagated to the consumer goods industries, especially those making durables and semi-durables, where it depressed employment and income and specifically attacked profit margins and, hence, again investment demand. This was the beginning of a downward spiral in which each turn generates the forces for the next one.

Once we had reached this stage, average costs, which were already being pushed up by wages, began to feel the additional impact of a contracting volume of output, which means that fixed and capital costs have to be spread over a smaller number of products. In modern technological conditions these expenses are so high as to weaken the firms' resistance under the threat of labour strikes. Thus the nature of the cost rise changed as the wage push broadened out into a general upward pressure on the costs of firms per unit of product.

Official estimates put gross investment in industry at 1,750 billion lire last year, a figure only just of the same order of magnitude as the 1,786 billion of depreciation assumed in the calculation of the net product of industry. Now, the completion of new plant last year swallowed up hundreds of billions of investment, and these are included in the 1,750 billion of gross investment; it follows that many firms cannot have invested enough to replace wear and tear on existing plant. This is indeed confirmed by a survey we did on costs and revenue in selected groups of industry.

This survey covered the movement of prices for the input of main raw materials and for the output in the form of goods produced, as well as labour costs in terms of wage rates and hours worked. The intention was to calculate shifts in the distribution of value added as between wage incomes and other incomes, a residual item which includes services, interest, depreciation and taxes.

The survey suggests that a large number of firms was probably unable last year to set aside adequate depreciation allowances. Given that the categories considered in the analysis were necessarily broad sectors, each of which includes technically more advanced firms which can more easily take the shock of the wage rise without losing their economic balance, the situation of the less well equipped firms must, in fact, be worse than the average income figures suggest.

In the group of engineering industries, the prices of basic raw materials fell by 5.8 per cent between 1961 and 1964; the prices of the products rose by 12.6 per cent and average hourly wages by 45.6 per cent. Allowing for the number of hours worked and for the actual output produced, one is led to conclude that the distribution of value added in the engineering industry underwent profound changes; in the sector as a whole the share of incomes other than wage income, including in this share services, interest, depreciation and taxes, seems to have dropped by 24 per cent per unit of value added. Such a sharp fall suggests that very many engineering firms set aside no depreciation allowances in 1964. Except, therefore, for those firms which have already gone through a technical renewal process, the future competitive strength of the industry is bound to be weakened by the ageing of its equipment.

The result of the survey so far as the textile industry is concerned are equally cheerless. The industry started out in 1961 from a position where keen competition had already reduced prices very close to costs and therefore had no margin within which to absorb the rise in labour costs per unit of product. Raw material prices have increased since then by 4.1 per cent, average hourly wages by 52.7 per cent and product prices by 15.8 per cent; the industry survived by producing the same output with a reduced number of working hours, dismissing workers from the less efficient factories.

In the metallurgical industry the prices of both raw materials and products fell, output rose by 8.5 per cent, while working time decreased by 1.3 per cent. The combined effect of these adjustments probably offset the rise in average hourly wages. Total income, other than wage income, per unit of value added rose by 4.4 per cent. However, it must be remembered that during the period under consideration a lot of new plant was taken into operation, which implies a considerable rise in the capital endowment of each worker. It follows that in this sector, which is in large part government-controlled, economic balance at the level of the firm really requires a larger share of value added to be imputed to the factor capital than in the past.

In the chemical industry, the price of base materials rose by 9.8 and that of the products by 8.2 per cent; average hourly wages went up by 50.4 per cent, the volume of output by 35.4 per cent and the number of hours worked by 1.2 per cent. In spite of the signal increase in productivity, there was an income shift to the benefit of wage earners. Both government-controlled and private companies in this sector have invested heavily and need to renew plant very rapidly; we are probably not far wrong, therefore, in guessing that the industry's profit and loss accounts are not sound—that it does not earn enough, in other words, to finance the renewal of plant to the extent necessary to keep competitive.

All in all, it seems fairly safe to conclude that, apart from those sectors in which major plant investment programmes started earlier reached completion, efficiency was last year furthered especially through organizational improvements, but that industry was unable to keep up the pace of technical advance which was so marked a feature of the preceding years. To do so, industrial firms would need more funds not only for plant renewal, but also for research.

Three years ago, in our Annual Report, we already drew attention to the change in the cost/benefit ratio; in the setting which I have now described, it would appear that this change is the principal cause of the fall in the level of investment and employment.

A policy of reflating demand through public works will no doubt contribute much to the improvement of our social overhead capital, but it can have induced effects on the level of investment only to the extent that the reduction of average cost by virtue of the distribution of fixed cost over a larger volume of output is not interrupted or offset by a further rise in labour costs. Labour costs per unit of output in industry, including building, rose last year by 9.4 per cent.

The steady growth of our economy depends upon its ability to re-equilibrate the economic position of firms. This is a necessary condition for preventing the deterioration of the machines to which the workers apply the factor labour; but it is necessary also for the viability of private firms which, unlike government-controlled firms, would otherwise find their credit-worthiness impaired.

It happens that particular firms are in great difficulties because they cannot get their cost/benefit ratio back into durable balance; to help such firms by credit privileges, however well-intentioned these may be and however much designed to alleviate hardships for the workers concerned, nevertheless delays the process of adjustment to an open economy and in the last resort damages total employment. If such rescue operations were to spread, if firms were at the same time not allowed to cut down their personnel to the extent necessary to make production costs competitive, and if obstacles were being placed in the path of concentration with a view to higher efficiency—then the effect would, without any doubt at all, be to weaken our economy's resilience, not to strengthen it.

When international competition prevents the price level from rising, the effects of a cost-push inflation can be corrected most quickly by lightening the tax burden on firms. Measures of this kind were recently introduced in Italy, but their effects offset only part of the increase in labour costs. Tax reliefs in connection with depreciation, on the other hand, are not particularly effective when firms do not earn enough, as is demonstrated by the fact that in many cases actual depreciation allowances fall short of the exemption limit.

Other countries have made their own experiences with economic growth. Some of them tried to force the pace of development by an indiscriminate expansion of demand; to this end additional productive activities, which could not have been financed by the flow of saving, were financed instead by credit from the central bank, or an expansion of money supply. This policy discouraged the supply of savings, but the relatively low interest rates greatly stimulated the demand for credit, and the resulting credit expansion set in motion a rising cost-price spiral which, among other things, diminished the real value of the credits conceded. As typically happens in an inflationary spiral, monetary expansion coincided with a general shortage of means of payment. Distortion in the direction of investment, waste of resources and rising costs ultimately undermined the whole economic system. The consequences for production were initially concealed by the fact that firms, with their unbalanced cost/benefit ratio, continued to produce, but cut down on their depreciation allowances. Plant became worn and obsolete; infrastructures, which were inadequate in any case, were not properly kept up. At this point the growth-delaying effects of this kind of policy became patent for all to see.

The Need to Strengthen the Financial Structure of the Italian Economy.— An economic plan for Italy is now undergoing final revision prior to its being tabled in Parliament. In substance, the intention of this plan is to overcome the imbalances in the Italian economy without detriment to the high degree of efficiency needed to stand up to increasingly keen international competition, but on the contrary by making good certain functional and cost-increasing deficiencies precisely through the elimination of imbalances—with particular reference to a number of fundamental infrastructures. This national plan is the fruit of a great effort to assemble knowledge and look into the future, in connection also with the medium-term projections worked out within the framework of the European Economic Community; as such, it naturally engaged our closest attention as regards its quantitative targets, the means by which it is proposed to achieve them, and, more specially within our field of competence, the connected problems of finance.

Unlike other national plans, the Italian one has the distinctive feature that it tries to analyse the financial investments of the various sectors of the economy. On our own part, we thought we could perhaps add something to the knowledge of these phenomena by constructing a sort of finance matrix, a tabulation showing flows of financial assets as between different sectors of the national economy, and the resulting mutual debit and credit positions. This presentation of data helps to interpret our country's experiences of recent years and it can be seen once more that the transfer of resources from one sector to another through financial channels comes up against impassable limits.

When, in a setting of incomes and taxation tending towards greater equality, the supply of shares and bonds exceeds the willingness to save in this form, stock prices fall and the public consequently becomes even more inclined either to spend its income, or at least to hold part of it in cash or in short-term credits expressed in terms of money. In both cases the financial structure and potential of the economy suffer. This process has been going on in Italy since 1961, though it lost some of its sting last year.

While the need for long-term finance funds increased uninterruptedly, the amounts that it was found possible to raise by placing security issues with the public did not change appreciably in absolute terms, and in 1963 even fell back. More especially, equity subscriptions by Italian residents remained at a rather modest level. As a result, the amount of long-term finance funds which had to be made available through the creation of money supply has been increasing from year to year: it was 648 billion lire in 1961 and 1,326 billion in 1964. This means that long-term credits for public works and investment in plant, and not infrequently to cover the current deficits of public agencies, had their counterpart in the primary and secondary liquidities owned by millions of ordinary people. This applied to 33 per cent of the economy's total long-term requirements in 1961, and to 47 per cent in 1964.

In economies which are not the scene of such large-scale structural changes as are coming to pass in ours, significant coefficients of correlation can be established between the growth of income and the growth of primary and secondary liquid assets; it is then possible to discover whether in any given period liquidity variations do, or do not, correspond to the norm. In our economy, the interpretation of these indicators is less certain, but we can hardly close our eyes to the existence of a liquidity/income ratio strikingly higher than is usual in other developed countries. On the other hand, this ratio has been rising uninterruptedly for many years, and this suggests that there are certain elements of stability in our economy's liquidity, which make some international experts' alarm seem somewhat exaggerated. It does, nevertheless, remain a baffling feature of our economy that so large a portion of the public's financial assets is in forms which allow owners to disinvest at once and without capital loss, whenever they decide that they want to spend more.

Now, an individual's decision to spend depends not only upon his stock of money and quasi-money and upon his income flow, but also upon the extent to which he can supplement both by selling other capital assets. A financial structure is all the more efficient, the more readily it enables securities to be sold without appreciably changing the level of interest rates. But there is a limit beyond which interest rates can be prevented from rising only by means of an increase in the money supply, and this has been happening in Italy in recent years. But while the increment of money supply could be absorbed in 1962 and 1963 by the reduction in our currency reserves and by a price rise which weakened the competitiveness of our goods compared with foreign goods, conditions have changed since then. At present, the impact on our currency reserves might well be even more serious, given that they now account for a smaller proportion of primary and secondary liquidities (7.3 per cent in 1964, as against 12.8 per cent in 1961); nor could the economy tolerate further price rises.

If this is correct, we must conclude that the manoeuvering space of monetary policy at present, and in the foreseeable future, is rather narrower than it was in 1961. It would be more risky now to intervene again, as we did in the fourth quarter of 1962 and the first quarter of 1963, to stem the fall in bond prices but at the same time overexpanded the economy's liquidity. Because of the sales of bonds and shares, and because of the private investors' widespread reluctance to subscribe to new issues of either, less securities were placed with the public than in earlier years. In 1961 the public had taken up 1,120 billion lire's worth of new issues, in 1963 it took only 840 billion, compared with 2,429 billion lire of total long-term credits to the economy; this means that only one third of the economy's long-term requirements was covered with the proceeds of security issues sold to the public. As a result we experienced inflationary phenomena which shook people's confidence in the stability of our currency and kept savers away from the bond market.

There are some institutional factors which, in Italy as abroad, create a tendency to employ more primary and secondary liquid assets in long-term credits. The banking system tends to exercise its intermediary function more and more in the sense of financing security purchases with deposits commanding a higher rate of interest, and this seems to be in line with the preferences of the public, which thereby obtains at the same time more liquidity for its capital and a satisfactory yield. There are also cyclical factors which, in Italy at any rate, tend to reduce the velocity of circulation of deposits. All this goes to confirm that the most urgent problem for the authorities concerned is to organize an efficient capital market, precisely with a view to hemming in the spreading practice of bond subscriptions through the creation of money assets.

Both in gross and in net terms, the volume of security issues has increased uninterruptedly since 1961: gross new issues amounted to 1,915 billion lire in 1961 and to 2,687 billion in 1964, and the corresponding net figures are 1,432 and 1,927 billion lire. The whole increment is attributable to bond issues; so far as share issues are concerned, it should be added that a good part of them was last year absorbed by non-residents taking a stake in Italian companies. Of the net total of 1,372 billion lire new bond issues in 1964, barely 298 billion were taken up by the public and insurance companies; the rest was placed with the credit system and the Social Insurance Funds.

A growing share of total bond issues is being floated on behalf of the Treasury and by E.N.E.L, E.N.I. and I.R.I.; between them, these accounted for 46 per cent of all net issues of fixed-interest securities in 1964. Furthermore, large portions of the requirements of these agencies and their subsidiary companies were financed by short-term credit during the last two years; given that this practice can hardly continue indefinitely, their bond issues must be expected to assume a much larger scale in the future. In these circumstances it is bound to become more and more difficult to make enough room for larger issues by industrial and other special credit institutes. Their new issues have remained at roughly the same level since 1962. Industrial credit operations both increased and underwent some change in geographical distribution, in so far as the share of credits extended to industries within the regional competence of the Cassa per il Mezzogiorno rose from 49 per cent in 1963 to 61 per cent in 1964.

The forced expansion of the volume of bond issues through liquidity creation raised the ratio of bond issues to national income in Italy to a level well beyond that prevailing in other countries of the European Economic Community. Nevertheless, all economic sectors complain of an insufficient supply of capital and of the high cost of such capital as is available—and yet interest rates are already kept down artificially by liquidity creation. These last few years a strange notion has been gaining ground to the effect that the capital shortage can be made good by conceding to this or that agency the faculty of issuing bonds and by encouraging those that already have that faculty to make large-scale use of it; the problem seemed to be merely one of promising contributions to interest payments. Autonomous agencies were allowed to commit expenditure before even having raised the necessary funds. It has also been suggested, finally, that capital for long-term loans could be raised directly from the Bank of Italy. Admittedly, the central bank regards the purchase of bonds issued or guaranteed by the government as one means to control the economy's liquidity, but I do consider it as my duty to point out how dangerous the above prescriptions could be.

The draft bill of the national economic plan is based on the correct assumption that the achievement of its targets is conditioned by an income distribution consistent with adequate formation of saving. Since it is not compatible with monetary equilibrium that firms should draw in outside savings solely through borrowing, relatively more capital needs to be raised on equity issues. Thus the problem of promoting the formation of institutional savings and their placement in shares assumes increasing urgency.

It is unfortunate that so little attention has been paid to the projects to set up investment or unit trusts, which could collect part of workers' savings and more especially those corresponding to the higher earnings due to the sliding wage scale. It is also disappointing, to say the least, that the long-standing proposals for rules to govern such investment or unit trusts still await approval.

During the first few months of 1965 the situation of the capital market has been showing some signs of improvement. Large bond issues have been placed with the public, and securities of earlier issues passed from the banks' into the public's ownership without upsetting bond prices. It should be noted in this context that when the central bank, or such agencies as get their liquid funds from it, buy securities they do so, and must do so, at the stock market price. These are temporary holdings, the ultimate objective always being, and remaining, their sale to the public whenever conditions allow. But equity issues have not as yet recovered, because the market does not yet appear receptive enough. If the conditions of the stock market are to be durably improved, firms must again be given a prospect of reasonable profits, so that they can gradually rebuild their capital structure—which, as we have shown, has been impaired in many cases.

During the fourth quarter of 1964 the indices of industrial production stopped their downward move, except in building and related activities; some other sectors began to display pronounced signs of recovery, which has been continuing early in 1965. There are also some indications that perhaps the profit and loss accounts of firms are beginning to get back into better shape. But I should warn that the improvements are by no means widespread and that they appear to be slow to take effect in the economy as a whole.

Such recovery as there is certainly owes much to the reasonable attitude of workers in those branches of industry which are most sensitive to cyclical fluctuations; if the trade unions follow suit, we should be able to look forward to a consolidation of these improvements. Meanwhile, the unions have become more intransigent in their dealings with the public sector. If their wage claims should further increase the current deficits of public agencies, the latter would ultimately become yet more dependent upon credits and would thus reduce the credit supply to the private sector still more.

The claims of public agencies in general, and of local authorities more particularly, on both short-term and long-term credit increased last year. At the same time, our usual survey of 500 major companies shows that firms in the public sector received relatively more net short- and long-term credit last year than did firms in the private sector. The total amount of short-term and long-term credit extended in all forms to the public sector (including autonomous government agencies, local authorities, other public agencies and government-controlled companies) was 1,528 billion lire in 1963 and 2,230 billion in 1964, when it accounted for 69 per cent of the year's total credits.

Gentlemen,

I hope I have made it clear beyond all doubt that unless firms in the public and in the private sector alike can get their earnings back into proper balance, we can expect no durable recovery of investment demand. Investment demand will grow, and will grow only, when this condition is fulfilled.

There are forces which work towards such a proper balance, and others which work against it. There is reason to believe that the former may prevail, but that their effects will be slow.

The national economic plan assembles a great body of knowledge about the fundamental aggregates of our economy, and indeed itself adds depth and refinement to this knowledge. It should, therefore, help the makers of economic policy to assess more accurately to what extent the choice of any given priorities requires alternative objectives to be sacrificed or cut back, as well as to adapt the distribution of means to the requirements of the public and the private economy. The plan also provides for an incomes policy based on the principle that the rate of increase of money wages should be close to the rate of increase of average productivity in the system as a whole; in its turn, the profit share is to be as high as is necessary to encourage investment. Some of the big trade unions, while not renouncing the use of their bargaining strength, say that in pressing their claims they will make due allowance for the needs of an open economy —and it is indeed much to be hoped and very important that this should happen on the occasion of the forthcoming renegotiation of national labour contracts. The bond market is more receptive and bank liquidity is high, so that firms should be able to raise funds for the introduction of such technical innovations as are necessary to keep efficiency up to the standards required by domestic and international competition. Higher activity in some sectors of industrial production should help to propagate the effects of a larger volume of output, so that firms can spread their fixed cost over a greater number of products.

On the other hand, we have now all but exhausted one element of flexibility which helped to keep average cost down in 1964, in so far as the margin of wage drift and fringe benefits has dwindled away. The disequilibrating sliding scale is still with us, even though it is not expected to go up by as many points this year as it did in 1964.

In these circumstances, an effective incomes policy is a necessary condition for raising economic activity to a level where our resources of capital and labour are fully employed.

I concluded my address to you last year on this occasion by saying that the difficulties encountered by our economy were not uncontrollable. Experience has indeed shown that they have been controlled. This year I regarded it as my duty to discuss certain trends which can help us to interpret some basic problems which face us right now. The structure of our economy was resilient enough to withstand the shocks of a sharp cyclical swing, but we sustained a serious loss of income. The progress of our society will be measured not least by the extent to which economic policy succeeds in any possible future downswing to minimize such losses by applying effective countermeasures in good time and with the informed support of all the groups concerned.

Our own duty is to maintain an orderly flow of credit and thereby to promote the spread of evergrowing supplies of working equipment, not least with a view to keeping together human resources which otherwise would have to disperse and look elsewhere for employment. But it is not everything simply to accumulate more machines and so to increase the stock of useful things which serve man; those who command the machines must also be given better living conditions. If we strive for this ideal our country will advance, thanks to our citizens' working capacity and notwithstanding temporary difficulties which experience shows can be overcome; it will advance, perhaps less fast than in the fifties, but, if we govern wisely, with more benefit to the whole nation.

X. *The Note Issue, the Bank's Balance Sheet and Profit and Loss Account.*

The Note Issue.— Having begun issuing the new series of 10,000 and 1,000 lire notes late in 1963, the Bank is now distributing, since December 1964, new 5,000 lire notes with a portrait of Christopher Columbus. This brings to an end that part of the modernization programme which concerned reducing the size of the notes and printing them by more modern techniques. There remains the problem of adjusting denominations to real prewar values. It has been stated more than once in previous Annual Reports that quite apart from the development of the market economy in Italy and from real income growth, the mere price rise since 1938 requires a change in note denominations.

The failure to reshape the structure of the note issue has had two consequences: an undue increase of notes in circulation, and a strong concentration on the highest denomination. In December 1964, 10,000 lire notes accounted for no less than 85.1 per cent of the total value of banknote and silver coin circulation.

The existence of so many notes is a great inconvenience to the bank of issue (and commercial banks as well), because much useless work and expenses are involved in printing and above all in checking, as well as counting, storing and transporting banknotes. The surfeit of notes furthermore impairs strict compliance with regulations and facilitates fraud.

The concentration on the big denominations concerns all those who use banknotes and constitutes clear evidence to the effect that the kind of money we have is out of step with the volume of transactions. The bulk of paper required for even a relatively small payment brings back the problem which in the past was one of the reasons why coins fell into disuse.

Early in 1965 the Central-Bank Committee of Members of Parliament and civil servants under the chairmanship of the Minister of the Treasury formally acknowledged the inadequacy of the structure of our note circulation and decided that improvements should be introduced as soon as possible. Accordingly the Bank has put in hand preparatory work for the issue of notes for more than 10,000 lire.

Given that the purchasing power of the lira is now roughly speaking one hundredth part of what it was in 1938, there is a strong case for starting with a 100,000 rather than with a 50,000 lire note, since it is not technically feasible to bring out both at the same time.

Other considerations also speak in favour of giving priority to the 100,000 lire note. There is statistical evidence that the denominations which are a power of 10 (100, 1,000, 10,000 etc.) are much more popular than those which are mere multiples of it (50, 500, 5,000, etc.); in 1938, 500 lire notes accounted for only 15.6 per cent of the circulation, and 1,000 lire ones for 31.9 per cent. The explanation probably is that in our decimal system it is easier to do mental arithmetic that way. This being so, the Bank's purpose of bringing about a quick and drastic reduction in the number of notes in circulation would not be best served by issuing the 50,000 before the 100,000 lire note.

It is, of course, quite likely that in the absence of 100,000 lire notes, those for 50,000 lire would be eagerly taken up by the public, but the subsequent appearance of the higher denomination would displace them from the market and drive them back to the Bank's counters. We would thus be simply wasting our resources on printing, checking, distributing and soon destroying notes which failed to fulfil the monetary function for which they were created.

Capital, Reserves, and the Profit and Loss Account.— No change occurred last year in the composition of the Bank's shareholders and, hence, voting rights. On 31 December 1964, the Bank's shares were, as a year earlier, distributed as follows.

72	Savings Banks	177,647	shares	with	468	votes
8	Public-law credit institutes .	54,500	»	»	141	»
3	Banks of national interest .	21,000	»	»	54	»
1	Social Insurance Fund . .	15,000	»	»	34	»
9	Insurance companies . . .	31,500	»	»	99	»
93	Shareholders	299,647	shares	with	796	votes
6	Savings banks	353	shares			
99	Shareholders	300,000	shares			

Ordinary Reserves, which stood at 4,955.1 million lire on 31 December 1963, rose during the year to 5,659.9 million. This was the result of appropriations of 131.6 million from 1963 profits and of 635.5 million investment income from the reserve fund itself, and a diminution of 62.4 million, which represents distribution to shareholders of part of the 1963 investment income from the fund (under Article 56 of the Statute).

Extraordinary Reserves rose from 2,664.4 million lire on 31 December 1963 to 3,028.3 million at the of 1964. This was the result of appropriations of 131.6 million from 1963 profits and of 265.9 million investment income from the reserve fund itself, and a diminution of 33.6 million, representing distribution to shareholders of part of the 1963 investment income (under Article 56 of the Statute).

Profit Appropriation. In application of Article 54 of the Statute, the Board of Directors propose, and the Treasury authorizes, the following appropriation of the Bank's net profit of 718.25 million lire for the year 1964.

	(million lire)
To Ordinary Reserve, 20 per cent	143.65
To shareholders, 6 per cent on capital	18.00
To Extraordinary Reserve, 20 per cent	143.65
To shareholders, a supplementary dividend of 4 per cent on capital	12.00
To the government, the residual of	400.95
Total net profit . .	718.25

In accordance with Article 56 of the Statute, the Board of Directors further propose a distribution to shareholders of another 34 per cent on capital, or 102 million lire, out of investment income from the ordinary and extraordinary reserve funds. This amount corresponds to 1.34 per cent of the overall reserves on December 31, 1964, and is, therefore, below the 4 per cent laid down in Article 56 as the upper limit of distribution under this heading.

THE GOVERNOR
GUIDO CARLI

BALANCE SHEET
AND GENERAL PROFIT AND LOSS ACCOUNT

BALANCE SHEET AS

ASSETS

Gold	L.	1,000,000,000,000
Cash in hand	»	21,638,446,092
Domestic bills of exchange	»	763,590,546,464
Bills for collection	»	203,965,767
Advances	»	284,747,076,359
Deferred clearing house payments	»	51,090,015,000
Foreign exchange balances abroad	»	64,074,156,694
Italian Exchange Office current account	»	2,068,830,455,006
Government or government-guaranteed securities	»	519,435,208,972
Premises	»	1
Miscellaneous debtors	»	305,320,350,553
Advances to the Treasury: extraordinary	»	410,000,000,000
Treasury current account	»	558,502,276,208
Miscellaneous services for account of government	»	28,678,471,970
	L.	6,076,110,969,086
Securities and other valuables deposited	»	4,918,115,478,886
	L.	10,994,226,447,972
Items written off in past years	»	241,097,808
GRAND TOTAL	L.	10,994,467,545,780

Audited and found correct - Rome, 12th May, 1965

The Auditors

ALESSANDRO BACCAGLINI
BRUNO DE MORI
MARIO MAZZANTINI
FELICE PAPPALARDO
RAFFAELE PILOTTI

The Accountant General

ARNALDO FALSINI

OF DECEMBER 31, 1964

LIABILITIES

Note circulation			L.	3,914,094,319,500
Bank drafts, cashier's cheques and other sight liabilities			»	57,463,303,534
Current accounts			»	118,689,645,537
Time deposits (incl. compulsory reserves)			»	1,459,430,012,242
Miscellaneous creditors			»	516,727,254,857
Net profit for 1964			»	718,247,065
Capital	L.	300,000,000		6,067,122,782,735
Ordinary reserves	»	5,659,858,268		
Extraordinary reserves	»	3,028,328,083		
				8,988,186,351
			L.	6,076,110,969,086
Depositors			»	4,918,115,478,886
			L.	10,994,226,447,972
Items written off in past years			»	241,097,808
GRAND TOTAL			L.	10,994,467,545,780

The Governor

GUIDO CARLI

GENERAL PROFIT

FOR THE

EXPENDITURE		
Administration and contributions to staff retirement fund L.	40,097,967,157	
Directors' emoluments »	316,058,118	
Transport of notes, coin and other valuables »	85,530,263	
Note printing »	5,089,589,088	
Expenditure on premises »	870,262,521	
		46,459,407,147
Circulation tax on notes and demand drafts L.	10,692,932,572	
Income and company taxes »	7,500,000,000	
Sundry taxes and dues »	518,584,462	
		18,711,517,034
Amounts written off L.		15,039,615,922
Interest payable »		7,411,610,838
Charity and other contributions »		104,459,435
L.		87,726,610,376
Net profit for distribution »		718,247,065
TOTAL . . . L.		88,444,857,441

APPROPRIATION

To Ordinary Reserve . . . .
To Extraordinary Reserve . . . .
10 % Dividend to shareholders . . . .
To the government . . . .

TOTAL DISTRIBUTABLE

Audited and found correct - Rome, 12th May, 1965

The Auditors

Alessandro Baccaglini
Bruno De Mori
Mario Mazzantini
Felice Pappalardo
Raffaele Pilotti

The Accountant General

Arnaldo Falsini

AND LOSS ACCOUNT

YEAR 1964

RECEIPTS

Discounts	L.	32,464,327,268	
Interest on advances	»	10,519,180,605	
Interest on other assets	»	25,708,263,687	
Commissions and custody fees	»	2,317,253,274	
Profits on foreign transactions	»	3,647,348,118	
Sundry profits	»	2,717,211,670	
			77,373,584,622
Interest on government securities	L.	10,750,518,042	
Revenue from real estate	»	320,754,777	
			11,071,272,819
		TOTAL . . . . L.	88,444,857,441

OF NET PROFIT

. . . .	L	143,649,413
. . . .	»	143,649,413
. . . .	»	30,000,000
. . . .	»	400,948,239
PROFIT FOR THE YEAR	L.	718,247,065

The Governor

GUIDO CARLI

THE ADMINISTRATION OF THE BANK OF ITALY

(1964)

BOARD OF DIRECTORS

Chairman: Guido CARLI * – Governor of the Bank

Paolo BAFFI * – General Manager

Tullio RICCIO * – Deputy General Manager and Secretary to the Board

Renato BRANZI
Gaetano CARBONE *
Carlo D'AMELIO
Gian Luigi DONES *
Antonio FONDA SAVIO *
Francesco MAILLER
Paolo MONICO
Lucio MORODER
Raimondo ORRU'
Giovanni POGGI
Eugenio VACCARI *
Ernesto VACCARINO
Giambattista VIRGA

* Member of the Executive Committee.

BOARD OF AUDITORS

Alessandro BACCAGLINI
Bruno DE MORI
Felice PAPPALARDO
Raffaele PILOTTI
Mario MAZZANTINI

ALTERNATE AUDITORS

Domenico AMODEO
Raffaele D'ADDARIO

THE CENTRAL ADMINISTRATION

MANAGERS

Giuseppe DE LIGUORI
Arnaldo FALSINI
Salvatore GUIDOTTI
Vincenzo ONORATELLI
Corrado PIROVINE
Carlo POSSENTI
Emilio RANALLI
Paolo VECCHIA